A Proposed Policy Blueprint for the ASEAN SME Development Decade 2002-2012

REPSF Project 02/005

Authors:
Choompon Asasen and Kanchana Asasen
Human and Organizational Potential Development Center (Bangkok, Thailand)
and
Nataya Chuangcham
Ariel Professional Management Services (Bangkok, Thailand)

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Preface

"Judge a tree from its fruit, and not from its leaves." Euripedes

The following policy blueprint, as proposed for the ASEAN SME Development Decade 2002-2012, was put together in a spirit of cautious optimism. SMEs can be leveraged into competitive, inter-linked and innovative businesses within and outside the region itself.

However, persistent efforts as well as changed mindsets among all stakeholders, both inside and across borders, are required to sustain and accelerate the transformation process. There are no durable short cuts or silver bullets for infrastructure establishment, entrepreneurship development, capacity building, innovation, regional co-operation, and durable competitiveness.

The blueprint was prepared under the auspices of ASEAN Secretariat and the Regional Economic Policy Support Facility of the ASEAN-Australia Development Co-operation Programme. We are deeply appreciative of the opportunity to work on a subject of significant interest and concern to us. Hopefully, this relatively bulky final product more than measures up to the Secretariat's commendable initiative and the Facility's invaluable support.

The unstinting comments and suggestions on our work from Dr. N. V. Lam, Adviser of the Foundation for International Human Resource Development (FIHRD), Bangkok, are gratefully acknowledged. His rich experience on the Greater Mekong Subregional economies, including the four newer ASEAN members, is reflected in several policy suggestions as well as in various implementation modalities for regional and subregional co-operation made in the policy blueprint.

Our thanks are also due to several persons in the ASEAN Secretariat – in particular, Ms Thitapha Wattanapruttipaisan of the Industrial Services Unit, Bureau of Economic Co-operation – for the courteous explanations on the terms of reference and many helpful discussions on various draft chapters of the blueprint. Useful suggestions on substantive and logistical matters were also received from Dr. Ramonette Serafica and Mr. John Cunningham of the Regional Economic Policy Support Facility.

As usual, high-quality and timely inputs continue to come from many of our colleagues. We must not fail to mention the dedicated and efficient assistance in research from Suthasinee Avapongpanich, Panthipha Iamsiriprida, Suntichai Inthornon, Supamas Sudhibud and Thanyalak Thewarajsomboon of Ariel Professional Management Services (APMS) and Human and Organizational Potential Development Center (HOPDC).

It is necessary to state at this juncture that the views and recommendations made in the policy blueprint are those of our own. They do not necessarily represent those of the ASEAN Secretariat, the Regional Economic Policy Support Facility, or the FIHRD.

Lastly, comments and suggestions on the policy blueprint will be received with thanks by all of us. Please forward them for our attention at <hopdc@thai.com>.

C. Asasen and K. Asasen (HOPDC), and N. Chuangcham (APMS)
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Policy Brief

Contents

Regional co-operation in support of the development and integration of SMEs will yield increasing social and economic returns within and across ASEAN. A competitive and innovative SME sector holds out enormous promise for the region, particularly in terms of:

- higher income growth,
- fuller employment of domestic resources,
- more gainful integration through global and regional trade and investment, and
- greater equity in access, distribution and development.

1. The Vital Contributions of SMEs

SMEs remain the largest source of domestic employment in most developed countries, and of non-agricultural employment virtually in all developing economies. Their presence can also be found across industries and sectors, domestic regions and rural locations, and urban and peri-urban areas. Moreover, they are an important vehicle for empowerment and participation -- especially of women, the young and other disadvantaged social segments.

Back to the basics. The renewed focus on SMEs among the regional economies in the aftermath of the financial and economic crisis of 1997-1998 gives grounds for cautious optimism. A the same time, a partnership among domestic, regional and extra-regional stakeholders in fostering SME sector development and integration is also no longer an option within ASEAN.

SMEs have long been the poor cousins of large firms in most parts of the world, ASEAN included. Yet, many of these big corporations and transnational enterprises had a more humble origin as SMEs at the initial stages of their operations several decades ago.

As well, clusters and networks of SMEs have driven the emergence of world-class industries. They have also revitalized domestic regions, which were in economic decline, in many parts of the world. In addition, most of the multiplying arrangements in global and regional production of the recent vintage have competitive SME suppliers as their unsung lynchpin.

By and large, private-sector SMEs are founded, owned and operated by individual entrepreneurs, often without much support from public and non-public resources. As such, they (rather than the large corporations) encapsulate the essence and enduring character of the market economic system. Indeed, entrepreneurial drive and private enterprise, in combination with judicious oversight from government, are even more important under the shifted paradigm in development (more below).

Other imperatives for SME promotion. A new development context has been ushered in by trade and investment liberalization in combination with rapid technological advances in many fields. These include information processing, telecommunications, transportation, bio-technology and engineering, and the new material sciences. As a result, there have been fundamental changes in the pace, patterns and processes of interaction within and between interdependent economies and enterprises.

Among other things, individual creativity and entrepreneurial initiatives are now coming to the fore in the management of change. But the paradigm shift has also underlined the importance of networks, linkages and alliances – and their widening and deepening within and across nations. SMEs are among the inevitable, if not always principal, stakeholders in the process.

Furthermore, there are other pressing issues for policy attention as well. First, SMEs will continue to be the socio-economic backbone of the region, although many segments of the SME sector remain burdened by limited skills and technological capabilities. Second, there remains a great shortage of medium-sized firms (or the "missing middle"), and this has severely constrained many efforts made to accelerate industrial deepening, upgrading, diversification and linkages among the regional economies.

Lastly, domestic output and employment has to be uplifted from the significant contraction caused by the 1997-1998 crisis, the 2001-2002 slowdown in global and regional economic activities, and the negative impact from of the severe acute respiratory syndrome in 2003. Meanwhile, additional job opportunities have to be created for the constantly expanding pool of workers (women, school leavers and university graduates etc.) and a business friendly environment, opened up for the potential and existing SME entrepreneurs themselves.

2. SME Development Approaches and Modalities

Collective action is needed to translate a great promise into actual performance – one which can be further replicated across industries and sectors and across the regional economies, too. The issue is not what to do, but how and where to start. The proposed blueprint for the ASEAN SME Development Decade 2002-2012 is a modest attempt in the above context.

Prerequisites of efficiency and competitiveness. Entrepreneurship is the foundation of gainful progress in the market economic system. Higher levels of efficiency and flexibility in product quality, cost and delivery punctuality are other determinants of sharpened competitiveness at the domestic and external levels. The upgrading process, largely pushed and pulled by innovation, can be further leveraged through the formation of inter-firm networks and linkages within and across borders.

Strategically, therefore, the SME sector must have, or must be assisted to possess, the critical attributes noted above. These characteristics of healthiness and dynamism, in turn, provide the main reference points for two of the following operational directions in the policy blueprint:

- One is the promotion of a culture of entrepreneurship, innovation and networking within the SME sector and, by extension, the domestic and regional economy at large.
- Two is to ensure that SMEs become and remain a learning organization – one in which productivity is constantly improved through knowledge-based and innovation-driven practices.

Thus, entrepreneurship development and capacity building measures at the national and regional levels feature prominently among the recommendations suggested in the policy blueprint. These measures include, notably, the proposed distribution of toolkit packages for self-diagnosis and trouble shooting of problems by SMEs themselves. Identifiable problems prevail, for example, in production processes, enterprise management, ICT-skills, and financial reporting and business plan preparations.

Other specific recommendations relate to the needs to speed up SME participation in borderless e-commerce. Indeed, the tremendous potential of "virtual" trade remains untapped by most enterprises, both large and small, in ASEAN. There are also additional policy suggestions to overcome major bottlenecks in bank and supplementary financing for SMEs. In particular, these suggestion concern credit rating and credit information systems, and the regionalization of financial resources and expertise.

Furthermore, due emphasis is given in the policy blueprint to the promotion of new and innovative modalities for industrial organization and co-operation. Indeed, the formation of SME clusters, networks and linkages within and across borders has definitely come of age. It represents an inevitable response to the push-pull influences of fiercer competition globally and regionally, of rapid technological advances, and of more sophisticated and exacting consumer preferences and market demands.

In the above context, SME readiness as participants in regional and global production networks and supply chains can be benchmarked under the code of conduct on subcontracting suggested in the policy blueprint. This proposed subcontracting compact is the same as an ISO 9000 certification for quality control and assurance. The importance of such a code or compact is not to be underestimated: many prerequisites for subcontracting are traditionally neither practiced nor expected by most SMEs in developing countries, including those in ASEAN.

SME-friendly governance. The public sector plays an indispensable, and evolving, role in sustaining a stable and equitable pattern of economic, social and, for that matter, SME development. An implied imperative in this regard is good governance and a conducive policy environment – especially in the promotion of entrepreneurial initiatives, private enterprise, on-going learning and innovation, and cross-border linkages and collaboration.

But the public sector has also become "leaner and meaner" along with the process of policy liberalization, administrative deregulation and asset privatization. Government agencies on their own are no longer a force which is sufficiently potent, adequately flexible, and necessarily well-endowed with resources in many developing economies, ASEAN

included. All these can be a significant weakness in an environment of constant and dynamic change in both substance and form.

As such, it is essential to ensure greater consistency, coherence and clarity in SME-related policies and programmes both across industries as well as within the public sector itself. Meanwhile, the needs for programme sustainability and maximum outreach entail an efficiency-oriented policy approach, greater policy focus, and better policy coordination in the delivery of SME-support and facilitating activities.

Undeniably, it is very difficult to eliminate conflicts in policy objectives and policy trade-offs across industries and sectors. Nevertheless, the policy blueprint identifies and discusses several inherent constraints and unintended biases which have served to crowd out the SME sector. Various policy options and proposals are then put forward in an effort to "crowd in" SMEs within the frameworks of governance.

Efficiency orientation and policy focus are among the guiding parameters behind many recommendations in the proposed policy blueprint. These parameters are explicitly embodied in capacity building proposals not only for SME in priority industries and sectors. They also serve to guide various suggestions for the strengthening of SME-support structures, financial sector institutions in particular.

In addition, the rationale and synergies in the division of labour between government and the private sectors are also presented in the policy blueprint. The framework for such a public-private partnership applies not only to the provision of business development services in favour of SMEs. It is also equally applicable to other joint endeavours, too. Indeed, improved public-private sector synergies ensure a better and more conducive configuration of policies and institutions for overall process of national and regional development itself.

3. Concluding Observations

The policy agenda for SME sector development and integration, as presented in the proposed blueprint, is extensive in scope and complex in its operational requirements. Certainly, the old issues and the new agenda cannot be resolved, carried out and accomplished totally and/or simultaneously in the short to medium terms.

But it is also well known that the removal of one set of barriers and problems is bound to create greater pressures and urgency to remove others. This can be expected sooner rather than later in a global and regional environment of dynamic transformation under the new development context.

Such systemic dynamics embody great opportunities for value-creation by all enterprises, both large and small. However, they also pose wide-ranging and difficult challenges to resolve at the national, regional and global levels. But the challenges have to be met because the competition for wealth-creating assets and opportunities has become greatly intensified across the world.

And that is the final message of this policy brief.

Executive Summary

Contents

Concerted efforts in support of SME development are no longer an option at the national and regional levels. This was indicated in the Policy Brief which also encapsulates, among other things, the increasing social and economic returns associated with SME promotion efforts.

1. Background and Context

The 1997-1998 financial and economic crisis induces a return to the fundamentals among economies in the region. Policy attention is again refocused on promoting SMEs, among other matters of concern. An eloquent manifestation in this connection, the ASEAN SME Development Decade 2002-2012, aims to accelerate and elevate collaborative action, at both the intra- and extra regional levels, for SME sector development and integration.

This proposed policy blueprint is intended to backstop SME-support measures and activities for implementation at the national and regional levels during the Decade. It was prepared under the auspices of the ASEAN Secretariat and the Regional Economic Policy Support Facility of the ASEAN-Australia Development Co-operation Programme.

The blueprint is organized in eight chapters although all the policy recommendations are made in Chapter Six. For ease of reference, however, table VI-1 in the same chapter indicates the complementarities between the policy blueprint and the Regional Action Plan for the Decade as mapped out by the ASEAN SME Agencies Working Group. In addition, brief annotations on the proposed pilot projects and on a selection of focal policy suggestions are listed in table VI-2 to assist in the consideration and prioritization process.

Chapter Six in the policy blueprint may thus be consulted first, as desired. But it is not a self-contained presentation. The guiding principles, rationale, context and background, and detailed justification for all policy recommendations made in Chapter Six are discussed at length in Chapters Two through Five.

2. Policy Issues, Implications and Approaches

The terms of reference for the policy blueprint are reproduced in Chapter One which also clarifies a number of other pertinent matters. These include the non-technical presentation and analysis of materials in this document, and the need for standardization of terminologies in business and development project planning and evaluation. The latter issue is discussed further in Chapter Seven.

Strategic and Operational Considerations. The policy blueprint, as stated in Chapter Two, is designed to facilitate the emergence of a SME sector which is characteristically entrepreneurial, growth oriented, outward-looking, modern and innovative.

Operationally, the proposed approaches and measures serve firstly to incubate a culture of entrepreneurship, innovation and networking among the regional economies and enterprises and, by extension, within the region at large. Secondly, they are also intended to ensure that SMEs become and remain a learning organization.

There is a vast number of SMEs which also differ significantly in terms of their own current and potential capabilities and competitiveness. The policy recommendations have thus to be guided by such parameters as:

- focus and targeting,
- efficiency and linkage orientation,
- the promotion of better synergies within the public sector, and
- improving the synergies and partnership between government and the private sector, in fostering SME growth and integration especially.

Current Conditions and the New Development Context. Chapter Three looks closely at several indicators of the intrinsic importance of SMEs as the economic and social backbone of ASEAN. These enterprises are the largest source of formal- and semi-formal sector employment. But most of them are far from modern, dynamic and inter-linked in their operations. Consequently, SMEs' contribution to output and exports is much lower than their relative importance in the economy.

Furthermore, as discussed at length in Chapter Four, SME development efforts are now further challenged by:

- fiercer regional and global competition, from China in particular,
- fast-paced technological progress and its equally rapid incorporation in products and production and marketing processes; and
- more sophisticated, demanding and constantly changing consumer preferences and market requirements.

But the new development context also embodies vast opportunities for value creation and capacity building by enterprises regardless of size. The process is mediated through:

- more gainful participation in trade and investment,
- easier access to the global store of knowledge and information, and
- greater integration into denser and deeper nexus of inter-firm linkages and other collaborative arrangements within and across borders.

Barriers and Biases against SMEs. Chapter Five examines in detail the main constraints on SME sector development and integration in the region. Among those constraints is the lack of a sustained track record in entrepreneurship development, and in product and process innovation. This was one of the issues behind the region-wide controversy as regards total factor productivity gains in the (pre-crisis) mid-1990s, and the regional crisis of 1997-1998 as well.

But SME capacity building is also necessary in a wide range of basic skills required for the effective and efficient organization and management of business undertakings. On-going enhancements in product quality, cost efficiency and delivery timeliness are particularly important in the above context; and so is adequate competence in information and communications technologies. The latter is a prerequisite for tapping the tremendous potential of e-commerce and also for gainful participation in inter-firm linkages and networking.

SME financing has been and will remain an intractable problem, not least because financial resources are typically in short supply virtually in all developing economies. Nevertheless, many financial support measures for SMEs have limited outreach at disparate cost. In addition, capital markets in the region are generally far from adequate for SME debt (bonds) and equity (shares) financing.

Higher transaction costs and the lack of expertise in the evaluation of SMEs render it unprofitable for commercial banks to focus on such enterprises as their main debt clientele. Meanwhile, most SMEs do not have a bankable business plan, which can reduce stringent bank demands for quality collaterals. Proper financial reporting and information disclosure is another difficult issue to resolve for many SMEs.

There are, at the same time, a large number of inherent constraints on and unintended biases against the SME sector policy areas. Their adverse impact tends to be more burdensome and costly because of the limited resources as well as operational scale of most SMEs. Among the wide ranging problems are:

- the scale-based “perverse” incentive syndrome,
- complex regulations and opaque discretion,
- policy changes without judicious sequencing and information dissemination,
- inadequate policy synergies (especially as regards coherence and consistency),
- the lack of sufficient transparency and effective coordination of policies, and
- limited evaluation of policy performance and impact

Recommended Approaches and Support Measures. A training-based programme in entrepreneurship development for long term implementation, along with a pilot short-term project, is suggested in Chapter Seven. Considerations of cost efficiency, programme sustainability and maximum outreach necessitate the generation of local capabilities in such training for the subsequent replication within and across domestic sectors and regional economies. In this context, considerable assistance to the four newer member countries is expected from ASEAN-6, at least in the short to medium term.

The same considerations of cost efficiency, programme sustainability and maximum outreach are also behind the recommended compilation and distribution of system packages (or toolkits) for self-reliant applications by SMEs themselves. These packages cover many generic skills in enterprise organizations and management. The pilot project, however,

focuses on the development of system toolkits for on-going improvements in product quality, cost efficiency and delivery punctuality; all these being the critical parameters of business competitiveness, comparative advantage and sustained inter-firm linkages.

There has been a serious and chronic lack of data and information on SMEs – in spite of their inherent socio-economic importance, and the recent re-focus of policy attention on the sector. Such a shortage has constrained severely the design and targeting of policy as well as the effective management of policy performance itself.

It is thus suggested, firstly, that surveys be carried out regularly to monitor, evaluate and benchmark the core competencies of selected SMEs in priority industries and sectors. This exercise also helps to identify shared areas of weakness for remedial capacity building on the supply side. A framework for the pilot survey project is presented, and related methodological issues discussed, in the policy blueprint.

Likewise on the demand side, an extensive list of the typical (non-negotiable) requirements on subcontractors from their regional or global clients can also be found in the blueprint. It is recommended, furthermore, that these pre-conditions be compiled and updated as a compact of subcontracting "best practices" to be expected from SMEs as well as for emulation and adoption by SMEs. This code of conduct or compact can serve as well to benchmark SME readiness, or otherwise, for match-matching and other inter-firm linkage purposes.

Extensive capacity building is needed by SMEs in business skills and operational capabilities for a fuller exploitation of the new technologies plus e-commerce. Such capacity enhancement is to be complemented, however, by the ancillary development from the public and/or semi-public sector of hard and soft infrastructure prerequisites which are of high quality, accessible and affordable. Such development and the related policy issues are generally of a long-term nature but the policy blueprint contains five transitional suggestions to facilitate and accelerate SME penetration of e-transactions within and outside ASEAN itself.

Again, many SME financing problems are also of a long-term nature. They are part and parcel of the development process itself. However, four recommendations are made in the policy blueprint to help resolve in the short to medium terms certain institutional weaknesses within the national and regional financial sector and environment.

On the supply side, proposals are made to strengthen institutional capabilities in credit rating and credit information systems. Demand side suggestions include better disclosure by SMEs of financial and other information, and adequate preparation of business plans by SMEs. Financial regionalization to widen the investor and resource base is also considered in the policy blueprint.

The discussion on a conducive policy environment for SME development and integration (in Chapter Five) leads on to seven suggestions. These focus on ensuring greater coherence and consistency in the design and sequencing of policies, and on better policy coordination and management. A framework for public-private sector partnership for SME growth and competitiveness is also presented in terms of the provision of business development services. However, such a framework is also suitable for consideration in implementing other joint programmes for SME support, as recommended in Chapter Six.

"What Gets Measured Gets Managed". Chapter Seven discusses the needs for better management of policy, programme and project performance, including those being put forward in Chapter Six. Policy impact measurement and assessment are an integral part of policy performance management. And the related parameters and benchmarks as well as methodologies for the process are then examined in some detail. A planning framework for the evaluation of policy performance is also given for illustrative purposes.

3. Final Remarks

The policy blueprint, as proposed, has over-delivered in relation to its terms of reference. But the production of a series of workable recommendations is not enough by itself, regardless of the possibilities for significant value creation implicit in their implementation.

This blueprint is not the work of a pressure group. It was put together in the enduring belief in entrepreneurial initiatives and individual enterprise, two essential characteristics of micro-businesses and SMEs in ASEAN and elsewhere as well. These business features constitute a cornerstone for durable and equitable socio-economic advancement -- given judicious oversight from government and a propitious environment in external development and co-operation.

The above belief, meanwhile, is also tempered by a parallel recognition – namely that SME sector growth and integration is an integral part of the overall development and transformation process itself. There are no easy quick fixes or magic bullets.

What is needed now is a firm and sustained resolve for action among all stakeholders, both intra and extra regional. The collective aim is to accelerate and elevate their co-operative efforts in support of SME sector development and integration both during and beyond the indicative timeframe for the ASEAN SME Development Decade.

In that context, Chapter Eight of the policy blueprint provides some suggestions on certain steps ahead for the operationalization of proposals and options selected or prioritised for implementation during the Decade.

Chapter One

INTRODUCTORY REMARKS

Contents

I. Overview

The development and integration of small and medium-sized enterprises (SMEs) do not take place in isolation. The process is part and parcel of a country's on-going efforts, firstly, to increase and diversify its economic structure as well as the amount and quality of its resources, both currently endowed and to be created. The second direction is to enhance the effectiveness, efficiency and flexibility of its business activities and services.

Domestically, a durable pattern of socio-economic growth, structural diversification and modernization, and quality enhancement will lead to higher levels of local value-added, greater productivity and further process flexibility. At the same time, gained technological and innovation capabilities will take place along with the formation and emergence of an increasing number of domestic clusters of enterprises, and denser networks of inter-firm linkages and partnering within and across border, too.

The positive and economy-wide effects from this process of overall development and transformation include higher domestic output and employment. There will also be improved capabilities and sharpened competitiveness at the regional and global levels. These productivity gains can be seen in domestic suppliers of goods and providers of services, many of which are bound to be SMEs themselves.

But a strengthened and diversified SME sector will also yield other substantial dividends (or positive "externalities") as well. In particular, there is the consequent reduction in rural outflows and other town-ward migration of people. This will lessen the heavy demand pressures on an increasingly limited and congested infrastructure, and on the increasingly degraded environment in the expanding cities and peri-urban areas of many developing countries.

A healthy and flexible SME sector will also help to sustain job creation, social cohesion and decentralized development, thus alleviating excessive and inequitable economic and regional concentration. Decentralization has been a policy priority long pursued with sustained vigour by government virtually across ASEAN and, for that matter, in most parts of the developing world.

Inevitably, SME sector development and integration are a holistic (integrated) and long-term process. It is predicated as well as generates a great demand on a variety of inputs at the national, regional and global levels.

There must, firstly, be a framework of conducive policies, adequately underpinned by laws and regulations. A synergic partnership between government and the private sector is essential, as is a propitious external environment. Secondly, a culture of entrepreneurship, innovation and networking has to be incubated. It is as necessary as a larger pool of workers who are suitably skilled, experienced and readily re-trainable.

The third set of inputs concerns the availability, accessibility, affordability and relevance of wide-ranging infrastructure and facilities, both hard and soft in nature. These requirements apply especially to those in credit and finance markets, education and training, business development services (BDS) etc. But they are also required for basic utilities such as telecommunications and transport networks, water and energy, research and development (R&D), and other productivity enhancing activities.

The nature and functions of the above inputs will have to evolve dynamically over time. The needs of economic actors and players, including SMEs, are continuously changing in volume, variety and intensity in response to the (spontaneous or induced) transformation and diversification of consumer and market demands. These demands are becoming more quality-conscious, sophisticated, demanding and, in many cases, service-oriented as well.

II. Terms of reference and blueprint structure

The following policy blueprint is proposed in support of the ASEAN SME Development Decade (ASDD) 2002-2012. It is designed to supplement ASEAN member countries' on-going efforts to foster and sustain SME sector development and integration.

The blueprint was prepared under the auspices of the ASEAN Secretariat and the Regional Economic Policy Support Facility (REPSF) of the ASEAN-Australia Development Co-operation Programme (AADCP). This programme is funded by the Government of Australia and the Facility component is executed by Melbourne University Private (MUP). The terms of reference (TORs) for the study are given in Box I-1 below.

Box I-1. Terms of Reference for the Proposed Policy Blueprint

The study will contain three key elements:

First, the context for SME development in ASEAN, containing an overview of a critical review and examination of the following:

a. The relative importance and contribution of SMEs to the domestic economy within ASEAN;

b. The various policy and non-policy constraints on and barriers against SME sector development and integration in the domestic economy of ASEAN; and

c. The emerging challenges to be managed and opportunities to be exploited by ASEAN SMEs under the new economy and the new competition, and related policy issues and implications to be dealt with by government within the region.

Second, a coherent set of conducive and supportive policy measures for SME sector development and

integration during the ASEAN SME Development Decade 2002-2012. Required features of the policy blueprint are as follows:

a. The policy measures will focus on strategic or focal areas for intervention, namely: access to market, finance, information technology, technology sharing, and human resource capacity building. However, suggestions on additional focal areas are also expected in the proposed policy blueprint. In addition, the formation and deepening of inter-firm linkages and networking are one of the major short-cuts (or bridgeheads) to domestic and international competitiveness. Thus, the study or the policy blueprint within it should furthermore list out the principal prerequisites and other preconditions for SMEs to serve as subcontractors and service providers or even supply partners to large enterprises or to transnational corporations. Such a list will help identify the common areas of weaknesses among ASEAN SMEs for remedial policy attention or for the conduct of training services in the promotion of inter-firm linkages and networking.

b. The policy blueprint should map out a number of the critical and forward-looking areas for further policy-based research and policy-oriented studies for the promotion of SME sector development and integration within ASEAN – with due attention being given to the opportunities and challenges to SMEs arising from rapid technological progress and intensified global competition.

c. The proposed policies should have a strong element of "regionality" or complementarities to national policy focus and priorities;

d. The policy blueprint should give due consideration to the different development conditions for SMEs among the older and newer ASEAN Member States, as well as emphasize the promotion of cooperation in SME sector development and integration between the older and newer member countries.

e. Feasible and actionable. The policy blueprint should be sufficiently specific in scope and detailed. Moreover, there should be a clear indication as regards the likely implementation timeframe for the suggested policy measures -- such as within the short-term (3 years or less), medium-term (from 3 to 5 years), and long-term (between 5 and 10 years).

Third, a methodology is to be suggested in the policy blueprint or in the study for an objective and systematic assessment of the short and long-term impact of various policy measures that are to be carried out under the ASEAN SME Development Decade 2002-2012 in support of SME sector development and integration within ASEAN. The proposed methodology must include:

a A wide range of indicators, benchmarks and parameters as regards SME capabilities and competitiveness as well as the prerequisites for inter-firm networking. This is necessary in evaluating the effectiveness of policy measures.

b. An assessment of the adequacy and comprehensiveness of data and information on the SME sector.

Organizationally, the proposed blueprint is presented in eight chapters (see Box I-2 below). The policy suggestions take full account of the current and emerging trends in domestic and external conditions; notably, all enterprises (both large corporations and SMEs) are facing a shifted paradigm in development. Due attention is also given to the socio-economic diversity within ASEAN in the framing of policy proposals (more on this later).

Box I-2. Structure of the Proposed Policy Blueprint

Chapter One introduces some contextual issues as regards SME development as well as the scope of the proposed policy blueprint. The mission statement and the guiding principles underlying the blueprint are specified at some length in Chapter Two.

The current conditions and characteristics of SMEs in ASEAN are then presented in the Chapter Three. This is intended to serve, among other purposes, as a backdrop for the three chapters to follow.

Chapter Four provides in broad brushes the "big picture" facing SMEs – with the focus being on the key challenges and imperatives of development under the new economy and the new competition. This is followed by a detailed examination, in Chapter Five, of the wide-ranging bottlenecks and constraints facing the SME sector in ASEAN.

A range of policy approaches, measures and options in dedicated support of SME sector development and integration is then suggested in Chapter Six. Many recommended measures and options can be selectively implemented at the regional level and others at the national level. Meanwhile, several others are suitable for implementation at both levels, too.

Chapter Seven is complementary to the cornerstone Chapter Six in that "What gets measured gets managed". It deals with the needs, process and parameters for better management of policy, programme and project performance. Some concluding suggestions as regards the next steps in operationalizing the policy blueprint are made in Chapter Eight.

III. A final note

It is necessary to clarify at this juncture that firstly, the proposed policy blueprint for the ASDD 2002-2012 is primarily designed to be user-friendly. The discussion of policy issues and implications in fostering SME sector growth and integration is necessarily based on a large number of research studies. But this is carried out in a non-technical manner, including in the terminologies used.

Secondly, the policy blueprint is not an academic exercise. Footnotes and references are unavoidable. Many relatively technical explanations and illustrations are relegated to footnotes and these account for many of the lengthy footnotes in the text. On the other hand, the double-column boxes in the text contain policy-related issues as well as other matters deserving due emphasis and highlight.

Thirdly, concepts and terminologies in business and development project planning and evaluation are relatively technical in nature. Indeed, a large number of them can be rather complex. At the same time, many of them have not always been used in a homogenous or uniform manner by stakeholders and development practitioners. This has often been a source of confusion and misunderstanding. It is a mundane task but still it is important to have some standard glossary of commonly used terms with simple and non-technical explanations for the non-specialists (more in Chapter Seven). Such a glossary will certainly be more useful than many high technical counterparts that are available, normally as Attachments, in textbooks and other professional publications.

Chapter Two

OBJECTIVES AND GUIDING PRINCIPLES

Contents

The policy blueprint for ASDD 2002-2012 contains a detailed justification, both conceptually and in operational terms, for a range of suggested approaches, measures and options. The major objectives and the guiding principles behind the proposed policy blueprint are the focus of discussion in the following chapter.

I. Mission statement

A. Strategic and operational levels

Strategically, the recommended policy blueprint aims at facilitating and sustaining the emergence and growth of a healthy and dynamic SME sector within ASEAN. Such a sector consists typically of co-operative networks and clusters of SMEs with linkages inside and outside the region itself.

Characteristically, many of these enterprises are entrepreneurial, growth-oriented, outward-looking, modern and innovative in product design and development. They are also more flexible in production and specialization, and effective and efficient in their use of inputs and other resources.

All these features are among the universal driving forces behind the durable effectiveness, efficiency, resilience and hence competitiveness of firms.[1] They have become even more crucial under the new economy and new competition. This is an environment of

[1] **Effectiveness** refers to the extent to which the activities of the firm contribute to the realization of its strategic plans and business targets, whether explicit or otherwise. **Efficiency** relates to the degrees of optimality or cost-effectiveness with which the firm's inputs are transformed into outputs. **Flexibility** denotes the speed with which the firm's activities evolve competitively in response to changing market requirements and expectations, whether or not such changes are foreseen or unpredictable.

on-going, rapid and often unexpected changes in both demand and supply conditions and circumstances.[2]

The new development context is also characterized by trust-based, inter-firm networking and partnering – collaborative linkages for better collective efficiency, more flexible specialization and enhanced innovative capabilities.[3] However, the new conditions and circumstances also emphasize entrepreneurial creativity and individual value creation in the management of change.

Operationally, the proposed policy blueprint for ASDD 2002-2012 is underpinned by two main considerations. One is to foster and sustain a local culture of entrepreneurship, innovation and networking. Two is to ensure that SMEs become and remain a learning and evolving organization (see Box II-1 below).

[2] Thus, competitiveness under the new development context depends on factors and forces several of which are of a non-price nature. One is the superior quality and reliability or the differentiated design of the products or services concerned. The second source of competitive advantage may be due to greater flexibility in production scheduling and in customized supply runs (or mass customization). The third factor relates to more timeliness and punctuality in delivery. Last but not least, the products and processes involved may embody greater social equity (in terms of workforce participation, employment conditions and workers amenities in the workplace) and better environmental compatibility (or friendliness).

[3] Innovation is used here in its broad sense. It refers to a process by which firms and entrepreneurs master or even improve on various elements or stages of the production and marketing process. Such a mastering and enhancement process is new to the firms and entrepreneurs concerned, irrespective of whether they are also new to their competitors or competing enterprises. The elements or stages involved in this process may pertain to input sourcing, skills base enlargement and deepening, design and production, the development of innovative or differentiated products and services, a diversification of marketing channels, the penetration of new market niches, the formation of inter-firm networks and linkages for increased collective efficiency etc.

Innovation as such denotes in particular, although not exclusively, a better way to do the same things – whether in terms of cost, time, quantities and combinations of resources used etc. Alternatively, it can refer to better, or larger volume of, products or services and/or improved cost-effectiveness in the production and marketing process obtainable from the same combination or quantities of inputs utilized previously. The emphasis is thus more on "software". This applies especially to the capabilities (a) to generate, learn and un-learn, absorb, adapt and enhance, and disseminate new technologies and processes; (b) to identify, organize, manage, and integrate as regards new business opportunities and niches; and (c) to interact, link and sub-contract, network and partner with and among firms for mutual gains in efficiency and flexibility, among other collective benefits. For further details, see Lam (1999).

Box II-1. Learning and Competitiveness

The meaning and implications of a competitive and learning organization (whether this is a big firm or a small enterprise) deserve some clarification.

At the national level, competitiveness is normally understood in business management as the extent to which the domestic environment (policy, institutions and infrastructure), in its totality, is conducive or detrimental to entrepreneurship, innovation, and business activities and initiatives.

Industry-level competitiveness refers to the extent to which an industry or sector has the potential for growth and/or to generate an attractive return on investment. These capital resources can be manifested as direct or portfolio investment flows. They can come from local and/or external sources which may be private, official or multilateral in nature.

At the firm's level, competitiveness is the effectiveness, flexibility and efficiency in the production and delivery of goods and services at lower costs than those of the competitors, or at a price premium over those from other enterprises. Such a competitive edge may be derived from several sources (see footnote 2 above). Nevertheless, it is supported and/or is leveraged and maximized by three main factors.

One is an on-going access to the available store of knowledge -- including that of a market, marketing and technology variety. Two relates to the large gains in collective efficiency and flexibility through participation (whether or not on an arm's length basis) in clusters of firms and/or in networks of inter-firm linkages. Such interactions can be backward with suppliers, laterally with other producers and providers, and forward with users and consumers.

The third element of competitiveness concerns the firm's own capabilities for on-going learning. This is a prerequisite for (knowledge-based and learning-driven) innovation – regardless of whether the process tales place in in product, process, organization and management within the enterprises and, by extension, in industries and sectors concerned.

Of crucial importance in the above context is the sustained and efficient provision from both the government and private sectors of relevant and affordable BDS and extension activities. And so is the generation and replication of appropriate local capabilities and infrastructure for such provision over time. All these are to meet the needs of an expanding, diversifying and more sophisticated SME sector in its development and integration processes.

B. Policy blueprint, development roadmap and regional action plan

The following Boxes II-2 and II-3 indicate briefly the inter-relationships and synergies among the above three documents for the ASDD 2002-2012.

Box II-2. Blueprint and Roadmap for SME Development

The policy blueprint suggested for the ASDD 2002-2012 can be regarded as an integral part of the roadmap for ASEAN SME sector development and integration.

Firstly, it has a set of objectives the realization of which, by and large, will contribute positively to the competitive growth and development of a healthy and dynamic SME sector in any economy.

For operational purposes, these objectives are then translated into a range of suggested policy approaches, measures and options. These policy proposals are characteristically focused, concrete and feasible for implementation within the decade.

Secondly, the recommended policy blueprint places a heavier emphasis on improving the capabilities and competitiveness of SMEs in the long-term. Such a competitive edge is to be achieved and continuously sharpened in two main ways.

One is through the on-going building up of human and technological capabilities, including through the targeted provision of BDS. Two is through the promotion, widening and deepening of enterprise networks, clusters and other inter-firm collaborative linkages within and across border.

In the above context, it is of great importance to ensure greater policy consistency, coherence and transparency. It is also highly essential to promote a synergic partnership between the public and private sector for SME sector development and integration. All these considerations are given due emphasis in the recommended approaches, measures and options in the policy blueprint.

It should be noted that the blueprinted approaches, measures and options so proposed pay special attention to the evident diversity among the older ASEAN member countries as well as between them and the newer member countries. The differences are particularly apparent in, among other things, economic and social conditions and circumstances within the region.

There is, for example, notable diversity in the pace and patterns of development, in economic and social development priorities and thrusts, in the timing and sequencing of structural transformation, in the flexibility in policy implementation and adjustment, and above all, in resource endowments and capabilities for on-going learning, upgrading and networking.[4]

[4] Within the region during 2001, for example, income per head of population was in the range of US$ 23,000-17,600 in Singapore and Brunei Darussalam. However, the corresponding levels were only US$ 2,800-2,000 in Malaysia and Thailand; US$ 1,000-730 in Philippines and Indonesia; and around US$ 400-255 in the newer ASEAN member countries.

Thus, the elements of regionality are reflected in the many proposed approaches, measures and options which can be pursued co-operatively across ASEAN; after all, the inherent differences within ASEAN can also be an important source of complementarities. On the other hand, several other recommendations are suitable for implementation initially within subgroups of member countries and then regionally, or at the national and then regional levels (and vice versa).

Box II-3. Policy Blueprint and Action Plan for the ASDD 2012-2022

An important input in the design of the proposed policy blueprint is the Regional Action Plan (RAP) for the ASDD 2002-2012. This plan was adopted by the Working Group of SME Agencies in March 2002.

The RAP contains a large number of recommended activities for ASEAN-wide implementation. In this context, the recommended policy measures and options in the policy blueprint are highly supportive of, or complementary to, the regional plan in several ways. This is well illustrated in Table VI-1 in Chapter Six.

One, the suggested policy blueprint provides the "big picture" or overall backdrop for the RAP. This applies especially in terms of the detailed discussion in the blueprint on several conceptual issues, guiding principles and the new development context relating to SME promotion and support (Chapters Two, Four and Five).

Two, the proposed policy blueprint also fleshes out and develops much further a large number of activities suggested for implementation under the RAP itself. These activities include, for example, SME entrepreneurship development, the promotion of inter-firm networking, the measurement and benchmarking of the capabilities and competitiveness of SMEs and so on (Chapter Six).

Three, the suggested blueprint also contains a range of other policy approaches, measures and options, which are not specified in the RAP. This can be seen in Table VI-2 of Chapter Six. Several of the suggestions are suitable for adoption or adaptation, as appropriate, for implementation under the regional plan. As such, the proposed blueprint adds more value and further comprehensiveness to the RAP itself.

II. Guiding principles

A change in both *perception and practices* – in other words, a new or different mindset -- is perhaps the most important element in sustaining SME sector development and integration in the coming decades. The reasons for this are discussed at length in Chapters Three through Five plus Seven.

In varying degrees, the need for attitude change applies top-down – including at different levels and layers of government, and across public-sectors too. Likewise, it is equally applicable at the grass-root levels, especially among SME entrepreneurs and managers themselves. In particular, certain traditional business practices and expectations are no longer applicable or viable under the new economy and the new competition.

Some of the elements which need changing are embodied in the guiding principles behind the policy blueprint for the ASDD 2002-2012. Other elements are examined at length in Chapter Four through Seven.

A. Facilitation

One, suitable SMEs can be identified, developed and leveraged into competitive and innovative enterprises operating at both the domestic and transnational levels. There is now a large amount of literature and numerous case studies on the emergence of competitive industries and the revitalization of domestic regions pushed and driven largely by networks and clusters of SMEs.[5]

The process has taken place in both developed and developing countries. It has often been induced and facilitated by support policy but there are significant instances of spontaneous development as well.[6]

Closer to home, there are many large firms as well as domestic and transnational conglomerates born and bred within ASEAN. These successful enterprises have long become household names with widespread "brand" recognition of the goods and services they produce or provide. However, most of them had a more humble and obscure origin largely as small-scale firms, often operating in smaller township, at the initial stages of their start-up just half a century or so ago.[7]

Generally, policy efforts to support and facilitate SME sector development and integration are not sustainable without great cost efficiency and effectiveness in the long run. This consideration requires the collaborative building up of local and regional capabilities in the provision of support and facilitation activities and services. It also implies closer ownership and participation of the target beneficiaries in the implementation and delivery process as well (see Box II-4 below).

[5] These development trends were spotted and subject to widespread attention particularly from the mid 1980s to the early 1990s. Between 1990 and 1996, for example, there were over 535 papers and publications in English alone on SME clustering, networking and related subject matters (Lam, 1997).

[6] See, for example, Liedholm and Mead (1998); UNCTAD and Gate (1993); and Sengenberger, Loveman and Piore, (1990) plus the extensive bibliographies cited in these publications.

[7] Notwithstanding his somewhat narrow perspectives and interpretations, Yoshihara (1988: 153-263) provides an interesting account of the stellar rise and transformation into large enterprises and transnational corporations (TNCs) of formerly small and family-owned or controlled enterprises in South-East Asia. In a related context, many famous corporations in the world and region – such as massive enterprises as Microsoft, Apple, Sony, Honda, Charoen Pokphand and so on started out as small companies.

Box II-4. Capacity Building for Cost-effective Replication

The proposed blueprint places much importance on the generation of local capabilities in key areas of SME organization and management. Such a policy approach is not just to increase the levels of regional and national self reliance as well as collaboration. It is also necessary to minimize over-dependence on costly external consultancy and advisory services.

In the process, therefore, the usefulness of resources invested from governments and donors for SME support are maximized. In turn, this will permit a re-direction or diversion of new or supplementary funding from one or both sources to more advanced or complex assistance in fostering SME sector development and integration.

Likewise, the facilitation measures suggested in the policy blueprint also envisage more direct ownership and greater participation of the SME beneficiaries -- including cost sharing in cash and kind, and resource pooling. As noted earlier, such a process is essential to ensure continuous involvement and improvement so that the participating SMEs become and remain a learning organization.

The policy blueprint contains an innovative approach in the above regard. This relates to the selective dissemination of a wide range of tool kits for self-diagnosis, self-reliant trouble shooting, and self-improvement by the SMEs themselves (see Chapters Five and Six).

The proposed approach above also represents a more effective and sustainable way to reach out to the largest number of the targeted SMEs. This consideration takes on special significance given the limited resources available to government (more below) and, on the other hand, the affordability, accessibility and relevance of BDS and extension activities available to SMEs from both the public and private sectors in most parts of the region.

B. Selective targeting

The second guiding principle is that focus and targeting are unavoidable.[8] On the one hand, no countries have the necessary resources for concurrent support of the massive number of their SMEs. These often amount to many millions (including micro-enterprises) in the larger, more densely populated and/or SME-intensive economies.

On the other hand, there are huge differences in the capabilities and competitiveness of SMEs within different sectors and industries. Firms in the top layers are likely to be more efficient, innovative, growth-oriented and outward looking. But they constitute a tiny

[8] A case in point in the context of focus and selection is the Dow Jones industrial averages. Movements in these averages have a profound influence on the financial and economic health, and safety of producers, consumers, workers, investors and lenders virtually across the globe. Yet, the averaged indices cover the share prices of just 30 (locally registered) corporations listed on the New York Stock Exchange (NYSE); admittedly, these are giant enterprises with extensive business activities transnationally. These 30 companies accounted for two-thirds (or US$ 10.1 trillion) of the total global market capitalization of all companies listed in the NYSE as at end-June 2002. This exchange, in turn, is equal to just over two-fifths of the market capitalization of all stock exchanges in the world. The Standard and Poor's Rating Agency 500 index and the Russell 2000 index, although larger in coverage, track the average value of still a very small fraction of the total number of operating enterprises in the United States.

minority – easily less than one per cent in terms of number, but with a much larger share in SME sector output, export and employment.

Thus, a focus on the top segments of SMEs in priority sectors and industries would greatly improve the chances of success of support and facilitation policies. Over the medium term (3 to 5 years), many of these SMEs can be expected to grow into a sufficient (critical) mass. Conceivably, they may also multiply and replicate across industries and sectors through the demonstration and other effects -- including inter-firm linkages and partnering, and geographical clustering.

Thus, the overall level of competitiveness and dynamism of all domestic enterprises as a whole will be raised higher as a consequence of SME sector development and integration. As noted earlier, such competitiveness and dynamism are the result of continuous upgrading and learning at the firm level as well as industry- and system-wide. They are as strong and durable as the weakest firms in the (primary and supportive) value chains (more in Chapter Five).[9]

Two issues need clarification as regards focus and targeting. One concerns the identification of priority sectors and industries. But this is not likely to be a problem, because most countries do have an appreciation of which industrial activities are of importance to them.[10]

The second issue is dynamic in nature. Production activities and services will not remain constant but will be evolving in terms of nature, scope and technological contents. In addition, new sectors and industries will emerge (and "sunset" activities decline) constantly in response to the impulses and imperatives from rapid technological advances and shifting complementarities among interdependent economies and regions.

As such, domestic enterprises (whether big or small) will have to evolve and adapt along the changing trajectories of economic growth, structural transformation and social development. Inevitably, the process will have to be induced or assisted, at least at the initial stages of evolving transformation and transition by business firms (see Box II-5 below).

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[9] Pertinent in this connection is the recent attention on national competitiveness and studies on competitiveness benchmarking. It reflects a growing appreciation that competitiveness is systemic in nature. Generally, competitiveness depends greatly on the synergies among sectors and industries and, on the other hand, on the framework of domestic policies and regulations. This is because the competitive edge and comparative advantage of a firm can be considerably or even totally negated in several ways. One, support and complementary activities and services along the production and marketing chain may be inefficient or inadequate (e.g., bottlenecks in transport and communications and other facilities, causing costly delays and more expensive inputs etc.). Two, there may be various biases as well as a lack of coherence and consistency in policy and regulation, imposing thus excessive transaction costs on the enterprises concerned. Three relates to the limited availability of information and facilities (particularly extension, training and trouble-shooting services) on a wide range of areas of crucial importance to learning, upgrading and hence productivity and quality enhancement.

There is a large amount of literature on the concept of, and policy implications from, "systemic competitiveness". See, for example, Esser *et al*. (1999: 62-85) and Altenburg *et al*. (1998) and the extensive references cited by them. Refer also to Porter, Sachs and McArthur (2001: 17-23) and Dawson (1997).

[10] By and large, the priority sectors and industries are likely to exhibit a number of typical features. Among them are high-levels of value added and technological sophistication, extensive inter-firm linkages (backward, lateral and forward within and/or across border), a heavy export orientation, and prospective economies of scale and scope.

Box II-5. Focus and Targeting in an Environment of Change

Several important implications arise in the above context (more details in Chapter Five). Firstly, there must be an evolving supply base of modern entrepreneurship, up-to-date skills in management (including for networking purposes), and technological capabilities.

Training in entrepreneurship development is given a heavy emphasis in the proposed policy blueprint. And so is the facilitation of SME capacity building through a largely self-reliant approach to maximize outreach at least cost, as discussed previously.

The second implication is the identification of potentially efficient and dynamic SMEs. Chapter Eight of the proposed blueprint contains a detailed framework for this purpose.

The framework is designed to ensure an objective, systematic and (statistically) robust assessment and benchmarking of SME supply-side capabilities and competitiveness. Given its innovative and pioneering nature, a pilot project is also suggested for testing as well as fine-tuning purposes.

Thirdly, it is equally essential to induce and promote new and innovative modalities and services in support of business enterprises, both large and small. Changes are clearly required on both the demand and supply side, as indicated in Chapter Five of the proposed policy blueprint.

Regarding financing, for example, it will be necessary for SMEs to provide standard financial information and adequately prepared business plans. Formal-sector financial institutions, meanwhile, must also improve their own capabilities for credit assessment of clients' financing proposals. There are no substitutes and short cuts in those connections.

As far as the provision of BDS and extension activities is concerned, the principle of "subsidiarity" embodies a rational basis for the functional division of labour between the public and private sectors. But such a division of responsibilities applies also to various levels and layer of government itself.

The fourth implication rests on a conducive policy and institutional framework whose availability is as critical as a synergic partnership for development between government and the private sector. This matter is examined further when the fifth guiding principle of the proposed blueprint is discussed later on

C. Efficiency, innovation and networking orientation

1. Efficiency

The third guiding principle in the proposed blueprint relates to the nature of policy intervention itself. As indicated previously, the suggested policy approaches and measures are largely oriented toward raising the efficiency, flexibility and competitiveness of SMEs. They are thus similar to the provision of fishing rods and related fishing skills to the concerned enterprises.

Thus, in nature, the blueprinted approach is not the same as the provision of the fish itself to the target beneficiaries. It differs significantly from many traditional SME-related policies, programmes and projects which are undertaken primarily for the purposes of welfare protection (or enhancement), and for poverty alleviation.

A welfare-based policy approach has its own deserved place within the overall policy and institutional framework of any economy. It is necessary to safeguard social equity, and to act as a social safety net in times of crisis or transitional adjustment.

But such an orientation has to be explicitly stated in terms of objectives and expected outcomes for the needed transparency and accountability in implementation, and for more accurate performance measurement and impact evaluation (discussed in Chapter Seven below).

It is also clear, however, that SME-related policy, programmes and projects with a primary welfare orientation are likely to be unsustainable on the desired scale in the long run. This is because of the massive number of SMEs on the demand side and, on the supply side, the huge and largely open-ended financial requirements and BDS associated with such a support approach.

Other issues with a largely welfare orientation include moral hazard and free-riding problems – difficulties which can be minimized or lessened through partial or total cost recovery from the target beneficiaries. As noted earlier, cost recovery and resource pooling is comparatively more feasible with SME support measures to be provided on a time-bound basis, and with capacity building for continuous improvement in efficiency and competitiveness as the major thrusts.

2. Innovation and networking

The fourth guiding principle is the incubation of a SME culture of innovation and networking. An efficiency-oriented approach, however desirable, depends for its success on a number of complementary and ancillary requirements. These prerequisites are considered at some length in Chapter Five.

Briefly speaking, consumer demands have become more sophisticated as well as constantly changing. As a result, competitive advantage on the demand side is increasingly determined by non-price parameters – such as quality, reliability, health and safety, social equity in production and marketing, and the environmental compatibility of products and processes.

Meanwhile, becoming the norm (rather than the exception) are shorter product cycles and smaller output batches, more frequent design changes, greater mass customization and just-in-time sourcing, and more exacting timeliness in delivery.[11] These supply side characteristics of competitiveness owe much to new and innovative modalities in the organization and management of production and marketing.

A major driving force in the above context is the proliferation of complex networks of international production (NIP) and cross-border supply chains. These arrangements break down the value adding process into more discrete functions and smaller activities. But they also ensure the consequent availability, to the participating enterprises, of proprietary information and technologies, and the subsequent access to demand sources and market segments.

Innovative technologies, marketing expertise and market access have long been a major constraint on SMEs. The new trends in industrial organization and co-operation have thus opened up additional opportunities for SMEs. In fact, NIP-related and supply-chain-based subcontracting and outsourcing cover highly sophisticated processing and manufacturing activities and services – including original equipment manufacturing (OEM) and more recently, original design manufacturing (ODM).[12]

ICTs have greatly widened not only access to information and knowledge; these being the driving force in organizational flexibility, productivity growth and sharpened competitiveness of enterprises. They have also reduced the costs of collaboration and linkages, both within and across border. Indeed, clusters or networks of inter-linked SMEs are behind most competitive supply networks that have proliferated globally in recent years (more in Chapters Four and Five).

The formation, widening and deepening of inter-firm subcontracting is thus an attractive and feasible bridgehead to durable competitiveness at the domestic as well as global levels (see Box II-6 below). The sustainability of such linkages is naturally conditional on compliance of the local firms to a large number of exacting requirements and other preconditions – especially those relating to cost, quality and delivery (Altenburg, 1999; Gereffi, 1999; and Humphrey, 1998).

On the flipside, however, enterprises and industries outside the NIP circuit or supply chains are likely to reach a plateau in quality, productivity and competitiveness. This is particularly true in R&D-intensive sectors and activities. In the worse-case scenario, they may encounter diminishing returns and stalled growth with the corresponding adverse impact on employment, investment, business confidence and innovation (Porter, Sachs and McArthur, 2001, p. 17).

[11] This is a transformation both facilitated and pushed by speedy progress in information and communications technologies (ICTs) and, on the other hand, by more fundamental forces and attitudes of a non-economic (or socio-cultural) nature in consumers' choice in the developed world and, increasingly, among the developing economies as well.

[12] Indeed, ODM has long been prevalent in the personal computer industry. The makers/distributors will provide performance specifications of the personal computers that bear their names or brand. However, they have little to do with both the design and manufacture of the products themselves. The same (sea change) trend is also occurring in the case of mobile telephone handsets – with Alcatel, Ericsson, Motorola and Siemens having outsourced ODM to Asian and other suppliers. However, the biggest global producer of handsets, Nokia (with a third of global sales), is still making the handset itself (McCartney, 2001: XI).

Box II-6. Prerequisites in Efficiency Enhancement and Inter-firm Networking

A major issue can be identified in knowledge-based and learning-driven improvements in SME efficiency, flexibility and competitiveness. It is the access of SMEs to BDS and extension activities. The proposed distribution of self-reliant toolkits, supplemented by related guidebooks and extension activities, is an innovative approach in the above regard, as discussed earlier.

But new and innovative ways and means have to be tried and tested in the provision of credit and finance in support of the SMEs' upgrading and diversification process. The required changes on both the financing demand side and financial supply side are also suggested in Chapter Five.

In another context, the sustainability of inter-firm linkages within and across border depends on SME capabilities to adhere gainfully to specific parameters and prerequisites. All can be compiled as a "subcontracting compact" or "code of conduct" for SMEs.

The compiled compact is useful for SMEs' capacity-building purposes. It is also required for a systematic, objective and comparable assessment of their readiness to participate in new or alternative forms of industrial organization and co-operation.

Meanwhile, further research is needed in the promotion of enterprise clustering. Chapter Six contains some specific suggestion in this connection.

A related issue in the promotion of inter-firm linkages is not whether to assist SMEs to invest in ICT-based facilities and services. Rather, it is how best to encourage SMEs to make the most cost-effective use of the new technologies.

In fact, ICTs are now a prerequisite for participation in the growing number of NIP and global supply chains. They are also indispensable for tapping e-commerce opportunities which have expanded tremendously in size and scope (more in Chapters Four through Six below).

C. Enhanced synergies between the public and private sectors

Government has a crucial role to play in fostering economic development and social transformation domestically and among interdependent economies. This applies especially to the promotion of private-sector participation and cross-border linkages to diverse nexus of healthy and dynamic industries, sectors and their constituent enterprises.

As discussed previously, one universal requirement in the above context is a good supply of the necessary hard and soft infrastructure and facilities; these have also to evolve timely, flexibly and adequately in response to growth and change over time. Such a provision, particularly by government, has a profound influence on business firms, including SMEs, as well as on the (local and external) markets for both of their inputs and outputs.

Meanwhile, government policies, institutions and regulations at various levels (macro, sectoral and micro) are needed for other equally essential purposes as well (Chapter Five). One, a judicious framework helps to build up trust and confidence as well as a culture

of entrepreneurship, innovation and networking among business players and actors, among other socio-economic strata.

Two, it is also necessary to facilitate entry and orderly exit, to promote competition and to prevent the abuse of dominant position, to protect of public health and safety, and to preserve and sustain ecological integrity. Three, structural adjustment and transformation have becomes more intensified under the new economy and the new competition. This implies concerted efforts to minimize transitional dislocations and costs, and to encourage resource relocation and the creation of new resources in the process.

As such, a conducive environment of policy, institutions and regulations is a precondition for durable, stable and equitable growth and transformation – including in SME sector itself. This has not often been so, however.[13] In addition, government has become "leaner and meaner" along with the process of policy liberalization, asset privatization and administrative deregulation virtually in economies of all shades of ideology from the late 1970s and early 1980s.

Thus, the fifth guiding principle behind the proposed policy blueprint concerns a durable and synergic collaboration between the public and private sectors, including in the promotion of SME sector growth and integration. For maximum efficiency and effectiveness, such joint efforts have to be conceived and carried out under well established, clear-cut, transparent and predictable guidelines and benchmarks.

[13] It is well known that by accident or default, SMEs tend to be discriminated against in a wide range of policies, the "perverse incentive" syndrome. In addition, the legal framework is typically complex while many regulations tend to be opaque. All these have increased considerably the transaction costs for SMEs, compared to those shouldered by their larger counterparts (more in Chapter Five).

Box II-7. Public-Private Sector Development Partnership

As discussed in Chapter Five below, the public sector on its own is, by and large, no longer a force which is sufficiently potent and necessarily well endowed with resources in most developing countries, including many within ASEAN. Moreover, programmes and projects under public-sector auspices are not always or adequately flexible to cope effectively and timely with the changing times.

In particular, SME financing has remained an intractable problem. Public sector institutions, by and large, are also not well known as a major source of innovations and productivity improvements. All these can be a considerable weakness under an environment of liberalized trade and fiercer competition, of fast advances in proprietary technologies and knowledge, and of constantly changing and more exacting demand conditions.

The synergies and (positive) externalities of public-private sector co-operation can be elevated through the principle of "subsidiarity". This refers to who can do what best -- as a complementary, a foundation-laying, or a reinforcing activity or service -- to those carried out by other players or actors. But the same rationale applies equally well in the functional division of labour at various levels and layers of government itself. Better coordination is yet another issue for attention (more in Chapter Five below).

Moreover, an improved partnership between the public and private sectors is essential for other important reasons as well. Joint consultation and implementation help ensure better policy coherence, consistency and transparency among industries and enterprises, across sectors and regions, and over the years too.

Closer interaction between the public and private sectors will also facilitate the first-hand gathering of data, information and other feedback so essential for better policy design, targeting, coordination and delivery (as discussed previously). In turn, these will raise the efficiency and effectiveness programme and project performance, and facilitate a more systematic and accurate evaluation of outcomes and impact (see Chapter Seven below).

Chapter Three

THE CURRENT SITUATION OF SME SECTOR IN ASEAN

Contents

Most of the founding members of ASEAN had achieved a striking record of "export success" in a wide range of primary commodities, processed agro-products, standard-technology manufactures, and tourism services in the 1970s and 1980s. However, a large number of these success stories have lost their competitive edge or have become "under-achievers" from the early 1990s.[14]

The erosion in competitiveness is due partly to the push-pull forces of policy liberalization and administrative deregulation -- those in the trade, investment and financial areas in particular. The pressures for competitive change have been further inflated by problems in capacity building, and in policy sequencing and implementation. All these contributed their share to the 1997-1998 financial and economic crisis in East and South-East Asia (more below).

I. An economic backdrop

Causally, the eroding competitive edge in many countries of the region is more deep-seated than just being due to falling productivity and, on the other hand, to inadequate product differentiation and ineffective quality upgrading. The latter two elements are among the main determinants of firm level competitiveness (Porter, 1990).

To begin with, there has been fiercer competition for the same markets and market segments from many new comers from both inside and outside Asia; the latter include Mexico under the North American Free Trade Agreement (or NAFTA). However, the most notable competitor has been China (more in Chapter Five).

In addition, severe constraints were encountered by policy efforts made by ASEAN to foster structural deepening and diversification into products and services of larger value addition, higher technology embodiment and greater levels of knowledge intensity. Part of the reason for this is the typical under-supply of sophisticated, broad-based, and competent inputs and infrastructure of a social and economic nature.

[14] For details concerning the historical patterns of revealed comparative advantage, see International Trade Center (1998: 180-181, 222-223, and 344-345) and OECD (2002: 138-142).

Such a shortage (in terms of access, affordability and relevance) constitutes an important barrier to the gainful growth and transformation of industries and sectors, and their constituent enterprises. This is because of definite socio-economic and ecological limits on the accumulation of ever-higher volumes of labour force and material capital stock in absolute terms. The same limits apply as well to the realization of ever higher rates of labour force participation and physical capital formation over time.

All these adverse developments and bottlenecks were behind the controversy as regards factor productivity during the (pre-crisis) mid-1990s (see Box III-1 below). They have also ignited across the region a widespread interest from the early 2000s in national and systemic competitiveness, especially the related studies on its evaluation and benchmarking.

Box III-1. Factor Productivity at the Enterprise Level

The improved efficiency per person employed with a given input of capital is also known as total factor productivity (TFP) gain. This was embodied in the so-called "Solow residual" (from a seminal piece of work published in 1957 by Nobel Prize Laureate R. M. Solow).

Recent publications have provided a sharper account of, and perspective on, endogenous process of macroeconomic growth and growth accounting. Generally, TPF gains depend significantly on sustained increases in national investment in non-material and ancillary.

The above applies, in particular, to investment activities and services for the development and diversification of (i) science and technology infrastructure, and R&D institutions; (ii) quality and productivity-enhancing programmes, and related training plus extension centers; (iii) design, testing and engineering facilities; (iv) marketing facilities and linkages, and access to market information; (v) new and innovative forms of organization and management, such as the clustering and networking of firms; and last but not least, (vi) a culture of entrepreneurship, innovation and networking.

TFP thus correlates positively with the availability of many attributes and characteristics of a "social" process. These are factors and forces which facilitate the timely and effective internalization of socio-economic gains (for example in infrastructure for education and technological development) as private or personal returns.

TFP became a widely controversial issue in many Asian tiger economies in the mid-1990s. This occurred after an attention-provoking exposition made by Krugman (1994) but based largely on a series of research results from Young (1994 and 1995). The controversy has spawned a series of subsequent research efforts and publications on this and other related issues by, for example, Mahadevan (2002), Barro (1998 and 1997), and Chen (1997).

Subsequently, two other adverse and counter-productive factors emerged in most parts of ASEAN during the 1990s. One was a cyclical contraction in global and regional demand for consumer electronics products, components and parts in the mid-1990s. Another was an excessive speculation from the early 1990s in real estate construction -- including in a large number of "prestige" office buildings and, to a lesser extent, residential and resort developments.

All these were taking place along with a much higher level of debt leverage and a much larger exposure to short-term debt denominated in foreign currency in many large corporations and business conglomerates in ASEAN and elsewhere, too. Meanwhile, deficits in the external current accounts were rising rapidly, thus leading eventually to a drastic (and unavoidable) fall in the exchange rate and then on to the financial and economic crisis itself.

The crunch in East and South-East Asia broke out on 2nd July 1997 with Thailand as the epicenter. The crisis was unprecedented in its severity as well as in its contagious effects.[15] But it has also served to induce a return to the basics (see Box III-2 below).

[15] GDP in several ASEAN member countries contracted, quite severely in 1998. Aggregate output was down by 7.5 per cent in Malaysia, 10.2 per cent in Thailand and 13.2 per cent in Indonesia. Comparatively, in the global economic downturn of 2001, GDP fell by 2.0 per cent in Singapore and went up by just 0.4 per cent in Malaysia (compared to an expansion of almost 10 and 8.3 per cent respectively in 2000). For details, see ESCAP (2000: 27-45 and 82-103; and 2002: 127-152).

Box III-2. The Economic Crisis and the SME Development Decade

The 1997-1998 financial and economic crisis brought with it significant setbacks to the trade and investment fronts. It also caused a substantial increase in unemployment and, in several cases, social instability in various parts of ASEAN.

The negative spillover effects were felt across the region, including among the newer member economies. Furthermore, the crisis has retarded somewhat the intra-regional process of economic complementation and integration. It has also diluted somewhat the pre-crisis eminence, especially in terms of political and economic clout, of ASEAN itself.

A striking economic turn around was registered in many parts of ASEAN over 1999-2000. The recovery process, however, was then abruptly derailed by the global and regional slowdown of 2001-2002. Largely as a result, several economies in East and South-East Asia have not regained their pre-1997 strength in terms of per capita income, the overall living standard and domestic employment levels, among other crucial parameters of socio-economic well being.

The 1997-1998 crisis has induced and resulted in a return to "the fundamentals" among most of the second- and third-generation "miracle economies" in Asia. Basically, it has contributed to a renewed focus on the SME sector, which was relatively neglected during the extended boom years. Such a policy shift was complemented with higher budget allocations plus substantial amounts of external aid in support of SME sector development and integration, including those made by Japan under the so-called New Miyazawa Initiative.

As such, SMEs are bound to feature more prominently in the subsequent patterns of economic growth and restructuring in many parts of East and South-East Asia. Indeed, the coming years of the new millennium may well be known as a decade of SMEs (Lam, 1999). The proposed ASDD 2002-2012 is a pertinent case in point in this connection.

II. The nature and characteristics of SMEs in ASEAN

On several social and economic grounds, SMEs are of overwhelming importance in virtually all ASEAN member countries – a fact which has been appreciated for many decades. In addition, the SME sector will remain the backbone of the region and, for that matter, of most countries in the world in the foreseeable future.

Indeed, the collaborative promotion of SME sector development and integration has been a major focus of policy within ASEAN as a group. It has also commanded much attention among the 21 developing and developed economies, spanning four continents, of Asia-Pacific Economic Cooperation (APEC) membership.[16]

[16] A Working Group of ASEAN SME Agencies has been functioning since 1995. APEC was established in 1989, and the first APEC SME Ministerial meeting was held in Osaka, Japan, in 1994. The APEC Ad Hoc Policy Level Group was first convened in Adelaide, Australia, in the following year and this Group was then converted into a permanent Working Group in 2000. However, SME issues are also considered by other APEC Working Groups as they are of a cross-cutting nature, especially in terms of their multi-sectoral implications and interdependence.

A. Nature

One, SMEs can be found in virtually every field of socio-economic activities and services -- in both urban and peri-urban areas, and across domestic provinces and regions within ASEAN. Micro-enterprises and, to a much less extent, small enterprises dominate overwhelmingly the SME sector in terms of number. By implication, therefore, a healthy and dynamic SME sector is important for durable stability and equity in socio-economic progress and regional advancement.

Two, SMEs cater largely for the local markets although a small number of them have been highly successful in their outward orientation -- as direct exporters, or as suppliers to domestic exporters and to NIP or cross-border supply chains. Notwithstanding this outward-oriented segment of the sector, SME production processes typically rely on labour-intensive and/or simple technologies, including in processing and manufacturing activities. Quality and packaging leave much to be desired as well.

Three, SMEs are, by and large, owned and operated by the (founding) entrepreneurs and members of their extended families. Indeed, the entrepreneurs themselves tend to play a crucial role in the success or failure of the SMEs concerned. Such a commanding influence, while understandable in terms of business development, can be a constraint in accessing finance from banks and venture funding sources (see Chapter Five).

But policy efforts to foster the on-going development of SME entrepreneurship and basic skills are even more important because of the changing development context. As noted earlier, this paradigm shift has been jointly induced by trade and investment liberalization at the global and regional levels. It has also been pushed by the rapid advances in ICTs as well as in transport, biology and new materials technologies (discussed in detail in Chapter Four).

Four, SMEs can be a useful vehicle for gender empowerment. In fact, women entrepreneurs have an important presence in the SME sector, according to a (study-cum-survey) report to the APEC grouping (APEC, 1999). Characteristically, women-owned businesses are also found in all major sectors of production and services. Their failure rate is not known, however (more on women-owned firms below).

B. Definition

There is a great diversity in the definition and classification of SMEs among countries within ASEAN and outside the region, too (Tables III-1A and III-1B). This is a reflection of the significant differences in aggregate income and its distribution, in production structures and capabilities, and in industrial and technological characteristics among economies. As such, there is no sufficient reason to expect that SME definitions be uniform or even comparable across countries and through time.[17]

On the other hand, the term SMEs has not always been understood in a uniform manner even within individual countries. This has posed difficult problems in the design, implementation, coordination and evaluation of SME-related policies. At the working level, in fact, such diversity has adversely affected the provision of credit, finance and other

[17] An interesting account of some of the main historical and other reasons behind the observed diversity in the defined "size" of an enterprise is given in Sengenberger, Loveman and Piore (1990: 5-7).

assistance to SMEs among agencies and institutions within the same country itself (Regnier, 2000, pp. 27-30; and Urata, 2000, pp. 157-158).

Dynamically, there is another consideration in favour of certain flexibility in the classification and definition of SMEs. This is to ensure that SME-related policies evolve along with the growth and transformation in domestic economic activities and structure, and in the technological sophistication and linkages of domestic firms within and across border (see Box III-3).

Table III-1A

Definitions of SMEs in Selected Countries in East and South-East Asia, 2002
Number of Workers and Capital Investment

	Number of workers	Capital investment (US$)
ASEAN		
Brunei Darussalam		
Small	less than 10 persons	-
Medium	11-100 persons	-
Indonesia		
CHI[a/]	1-4 persons	-
Small	5-19 persons	-
Medium	20-99 persons	-
Malaysia[d/]		
SMEs	less than 150 persons	-
Myanmar[d/]		
Small	10-50 persons	less than 148.6 thousand[f/]
Medium	51-100 persons	148.6 to 742.9 thousand[f/]
Philippines		
Cottage	1-9 persons	1.9 to 28.8 thousand[h/]
Small	10-99 persons	28.8 to 287.9 thousand[h/]
Medium	100-199 persons	287.9 to 1.15 million[h/]
Singapore		
Manufacturing	less than 100 persons	less than 0.8 million[i/]
Services	less than 200 persons	less than 0.8 million[i/]
Thailand		
Manufacturing and services		
Small	less than 50 persons	less than 1.7 million[j/]
Medium	51-200 persons	1.17 million to less than 4.67 million[j/]
Wholesale trade		
Small	less than 25 persons	
Medium	26-50 persons	
Retail trade		

	Number of workers	Capital investment (US$)
Small	less than 15 persons	
Medium	16-30 persons	
Viet Nam		
Small	less than 30 persons	less than 65 thousand
Medium	30 to 200 persons	65-260 thousand
Non-ASEAN		
China		
Small	50-100 persons	
Medium	101-500 persons	
Japan		
SMEs		
Capital-Intensive [k/]	less than 300 persons	
Wholesale	less than 100 persons	
Retail	less than 50 persons	
Small-scale Enterprises		
Manufacturing etc.	less than 20 persons	
Commerce and Services	less than 5 persons	
Republic of Korea		
Capital-intensive [m/]	less than 300 persons	
Construction	less than 200 persons	
Commerce and services	less than 20 persons	

Table III-1B

Definitions of SMEs in Selected Countries in East and South-East Asia, 2002
Value of Assets and Annual Sales

	Assets (US$)	**Annual sales values (US$ million)**
ASEAN		
Brunei Darussalam		
Small	-	-
Medium	-	-
Cambodia [b/]		
Small	75,000 to less than 0.25 million	
Medium	0.25 million to less than 1 million	
Indonesia		
CHI[a/]	-	-
Small	less than 20,000 [c/]	less than 0.1
Medium	20,000 [c/] to 50,000 [c/]	0.1 to 5 million
Malaysia [d/]		
SMEs	-	less than 6.6 million[e/]
Myanmar [d/]		
Small	-	Up to 0.3 million
Medium	-	0.3 to 1.5 million [g/]
Philippines		
Cottage	-	-
Small	-	-
Medium	-	-
Singapore		
Manufacturing		
Services		
Thailand		
Manufacturing and services		
Small		
Medium		

	Assets (US$)	Annual sales values (US$ million)
Wholesale trade		
Small	less than 0.7 million[j/]	
Medium	0.7 million to less than 1.4 million[j/]	
Retail trade		
Small	less than 0.7 million[j/]	
Medium	0.7 to less than 1.4 million[j/]	
Viet Nam		
Small		
Medium		
Non-ASEAN		
China		
Small		
Medium		
Japan		
SMEs		
Capital-Intensive[k/]	less than 0.83 million[l/]	
Wholesale	less than 2.49 million[l/]	
Retail	less than 0.08 million[l/]	
Small-scale Enterprises		
Manufacturing etc.		
Commerce and Services		
Republic of Korea		
Capital-intensive[m/]	1.65-6.61 million	
Construction		
Commerce and services		

Source: Hall (2002, pp. 9-10), Myint (2000, p.3), Reguier (2000, pp.30-31), SMIDEC (2002, p.5), Tambunan (200, pp. 29-30), and Ministry of Industry, Mines and Energy of the Kingdom of Cambodia.

a/ Cottage and household industries.
b/ Manufacturing sector only; assets excluding land.
c/ Excluding the value of land and building.
d/ Manufacturing firms and manufacturing-related service enterprises only.
e/ Exchange rate of local currency: 3.8 per dollar.

f/ Official exchange rate of local currency: 6.73 per dollar as of May 2002. Market rate of exchange: 952.5 per dollar (as of September 2002) thus equivalent to US$ 1,050 for small enterprises, and between US$ 1,050 and US$ 5,250 for medium-scale enterprises.

g/ Annual production value converted according to the official exchange rate (as above). Conversion with the market rate will yield US$ 2,625 for small enterprises, and between US$ 2,625 and US$ 10,500 for medium-scale enterprises.

h/ Official exchange rate of local currency: 52.1 per dollar as of September 2002.

i/ Official exchange rate of local currency: 1.8 per dollar as of September 2002.

j/ Official exchange rate of local currency: 42.8 per dollar as of September 2002.

k/ Official exchange rate of local currency: 15.3 thousand per dollar as of September 2002.

l/ Official exchange rate of local currency: 120.37 per dollar as of September 2002.

m/ Official rate of exchange rate of local currency; 1,210.3 per dollar as of September 2002.

Box III-3. Some Issues in Classifying and Defining SMEs

There is room for flexibility and evolution in the above process and procedure.

Firstly, the levels of capital intensity required by firms differ significantly in different industries and sectors. Those in capital-intensive manufacturing (metal tools, metal and wood processing) and sophisticated service will need comparatively a much larger amount of investment in machinery and equipment.

Likewise, there are different levels of labour intensity involved in different production and service activities. The production of garments, toys and shoes, and other assembly activities rely on a large number of workers in relation to capital investment and sales values. In comparison, many high-tech services – such as high-quality printing, computer graphics and soft ware development, and website design – are much more capital intensive per worker employed.

Thus, many firms may not be regarded as belonging to the SME sector at all on some criteria. However, they are SMEs on the basis of other criteria. Such a complexity will pose continuing difficulties in the design, implementation and coordination of SME-support policies, and in the evaluation of their impact as well.

Secondly, SMEs are lumped together and defined as one category of firms in some countries. While this simplification is good for operational purposes, it also tends to obscure two important parameters. One is the large gap of capabilities and competitiveness between these two classes of firms. Two is the "graduation" from small to medium-scale enterprises. Such a process is of great significance to the design and focusing of SME-related policies.

It may, therefore, be necessary to break down the aggregation into two sub-categories of firms simply for the purpose of information and data collection. This serves to provide standardized inputs for more effective policy management, coordination and evaluation.

Thirdly, growth and change will create further problems in classification. After all, economies are constantly expanding in terms of income and employment, the skill base of workers, and the technological sophistication as well as the structure of production and services itself.

As such, SME definitions and classifications will have to evolve over time to better reflect changing social, economic and sectoral conditions and circumstances. Periodic revisions (e.g., every 5 or 10 years) are thus necessary to ensure a durable degree of consistency and coherence in SME-support policies, programmes and projects.

C. Economic characteristics

Generally, the data and information on the SME sector are not as up-to-date and as extensive as could be desired virtually across the developing region. The shortage is both acute and chronic. It has persisted despite the intrinsic importance of SMEs and the renewed policy focus on them in recent years. This significant weakness in statistical service has imposed another constraint on policy design and impact assessment.

In particular, the shortage is particularly evident in terms of the sectoral and industrial composition of SMEs; SME inputs and turnovers; and the contribution SMEs to income, employment and exports. Information is also lacking regarding the characteristics of domestic clusters and networks involving SMEs; the nature and relative importance of local and external linkages and alliances that SMEs maintain with their suppliers and customers as well as with technology and productivity-enhancing institutions and so on.[18]

Generally, the available information and data show clearly that, firstly, SMEs are "massive" in terms of number in most countries, even with the exclusion of micro and agriculture enterprises. In fact, the SME sector consists of millions of firm in several countries (Table III-2).

Secondly, SMEs account for the large bulk (upwards of 90 per cent) of the number of all private-sector firms within ASEAN (Table III-3). Thirdly, they also employ an overwhelming proportion (75-90 per cent) of the domestic workforce, especially young persons and women (APEC, 2000).

In the above contexts, women own and operate around 30 per cent of business firms in the formal sector in such countries as Indonesia, Philippines and the Republic of Korea (APEC, 1999). However, these enterprises tend to be "younger" in terms of the age of their establishment and the period of their operations. They also have relatively fewer employees than the average SME.

By and large, women entrepreneurs have unanimously expressed a strong desire to build up their business capabilities and competitiveness. They are particularly eager to undertake capacity building measures and undergo the necessary training in management and organization skills, and in productivity and quality enhancement processes. The self-reliant toolkit system approach in the proposed policy blueprint is especially pertinent in the above regard.

[18] For a more detailed discussion on the lack of serial and comparable data and information, see Hall (2002: 12-17), Regnier (2000: 35-37), ILO (1997: 36-37), Hill (1995), and APEC (1994a and 1994b).

Table III-2

Number of Non-agriculture SMEs in Selected East and South-East Asian Countries, various years (In thousand)

	Actual 1990	Actual 1996	Estimated 2000
ASEAN			
Brunei Darussalam	3.8	4.1	5.0
Cambodia	n.a.	25.3	25.4
Indonesia [a/]	12 045.6	16 416.0	16 000.0
Lao DPR	n.a.	n.a.	n.a.
Malaysia	n.a.	18.9	19.0
Myanmar	n.a.	34.4 [b/]	n.a.
Philippines	77.8	99.8	81.8
Singapore	31.5	47.0	54.0
Thailand	n.a.	311.5 [c/]	350.0
Viet Nam	1.0	30.0	200.0
NON-ASEAN			
China [d/]	8 608.2	7 253.4	8 000.0
Japan	6 484.3	6 433.6	6 139.7
Republic of Korea	2 094.6	2 677.1	2 700.0

Sources: Hall (2002: 12); Myint (2000: 5); Regnier (2000: 24); Tambunan (2000: 28), and Ministry of Industry, Mines and Energy of the Kingdom of Cambodia.

Notes: a/ Small enterprises in agriculture numbered some 22.5 million in 1996.
b/ As of January 1998.
c/ 1997.
d/ Including state-owned SMEs.

Table III-3

Relative Importance of Non-agricultural SMEs:
Size and Employment in Selected East and South-East Asian Countries, 2000[a/]

	SMEs as % of all firms	SME workforce as % of total employment
ASEAN		
Brunei Darussalam	98	92
Cambodia [c/]	99	45
Indonesia	98	88
Lao PDR	n.a.	n.a.
Malaysia	84	39 [c/]
Myanmar [b/]	96	78
Philippines	99	66
Singapore	91	52
Thailand	96	76 [c/]
Viet Nam	96	85
NON-ASEAN		
China	99	78
Japan	99	78
Republic of Korea	99	73

Sources: Hall (2002: 12 and 26), SMIDEC (2002: 5), Myint (2000: 5), Regnier (2000: 23), and Ministry of Industry, Mines and Energy of the Kingdom of Cambodia.

Notes: a/ Estimates.
b/ 1998.
c/ Manufacturing sector only.

Meanwhile, the relative share of SME production in total domestic output is disproportionately smaller, generally in the range of 20-40 per cent in East and South-East Asia. In addition, the direct contribution of SMEs to merchandise export earnings is likewise small, typically some 15-25 per cent.

Furthermore, is the narrow range of SME exports, plus the low value-added of those destined for external markets. Food products, textiles and garments, leather goods, furniture items, and handicrafts feature prominently in such exports. These categories account, in particular, for the bulk of SME export earnings in several countries – including Indonesia, the Philippines and Viet Nam.

Of equal concern is the hollowness in the industrial structure, a typical weakness in virtual all developing economies. Box III-4 below examines this matter in greater detail.

Box III-4. The Missing Middle

Medium-sized firms constitute only a very tiny segment of the SME sector at present. They are likely to be less than one percentage point in terms of number, although not so on the basis of their relative share in SME sector output and exports.

As a result, the industrial structure remains characteristically "hollow" in most parts of ASEAN and elsewhere as well. This "missing" middle reflects, among other things, the absence of a dynamic core of mid-range enterprises or of supporting industries.

This "hollowness", in turn, mirrors the lack of dense networks of domestic clusters of firms and of inter-firm linkages. These alternative (and relatively new and innovative) modes of industrial organization and co-operation yield considerable collective gains in economic efficiency, flexibility and competitiveness (more in Chapter Four).

The mutual benefits can be reaped by SMEs within the concerned clusters and networks. They also accrue to both SMEs and their collaborating conglomerates of business and TNCs (Altenburg, 1999; and UNCTAD, 1988: 15-20).

The above considerations reinforce further a guiding principle for the proposed policy blueprint (noted in Chapter Two). This relates to the need for policy focus on, and targeting of, SMEs in the top segments of capabilities and competitiveness in their own industries and sectors.

In particular, efficient firms allow other enterprises to purchase inputs more cheaply. Dynamic and innovative firms induce others to keep up with the latest technologies in production, management and organization. Flexible enterprises speed up the capabilities to respond quickly in other firms which have backward, lateral or forward linkages to them.

Chapter Four

THE NEW DEVELOPMENT CONTEXT FOR SMEs

Contents

To reiterate, there are solid grounds in support of co-operative and persistent efforts to foster SME sector development and integration in ASEAN (see Box IV-1 below). This is a challenging development process, as will be examined at length in the following chapter. The discussion also serves as a backdrop for a detailed examination of the constraints and bottlenecks in SME sector development and integration (Chapter Five), and for the set of policy measures and options suggested in Chapter Six of the policy blueprint.

Box IV-1. Pressing Needs for SME Development

One, the over-whelming and inherent socio-economic importance of SMEs implies increasing socio-economic returns through SME supportive efforts among individual ASEAN member countries as well as within the region itself (Chapter Three).

Two, there is the significant shortage of medium-sized firms in ASEAN industrial structure. SME development efforts will help to fill in gradually such "hollowness", which has long been a critical constraint on structural deepening and diversification, technological upgrading and inter-firm linkages, among other things (Box III-4 above).

Three, a renewed push in support of SME growth and competitiveness is no longer an option. It is needed not just to underpin a more speedy and durable recovery from the significant contraction in employment and output from the economic crisis and slowdown of the past few years. Equally pressing is the creation of adequate employment opportunities for the constantly expanding pool of prospective job seekers (especially the young and female workers), and for the potential SME entrepreneurs themselves (Chapter Three).

Four, SMEs and, by extension, all business firms have to manage growth and change in a new and more challenging development context. To begin with, there is the significant intensification in global and regional competition.

In addition, the competitive trends above are compounded by the rapid incorporation of fast-changing technologies in production processes and products. Meanwhile, consumer preferences and market demands have become much more sophisticated and are constantly changing as well. These are among the focal matters to be discussed in Chapter Four below.

I. Overview of development challenges

Globalization and the new economy have altered fundamentally the pace and patterns of economic interaction among the involved players and actors, including large firms and SMEs, within and across interdependent nations. One, the levels of knowledge intensity in production and marketing have risen significantly under the new economy. Two, business competition has meanwhile become much fiercer while market demands, more exacting and sophisticated across regions of the world.

These push-pull forces have necessitated further policy liberalization, administrative deregulation and structural transformation. Such efforts are increasingly essential to mobilize and retain (external and local) resources needed to improve the local supply base, domestic competition, systemic productivity, and hence external competitiveness.

The above process, however, has become even more complex for another reason. The liberalization of cross-border trade itself carries with it demanding commitments. By default perhaps, it has tended to be more technical in substance as well as highly legalistic (or "lawyer-intensive") in practice. All these have imposed thus another heavy burden on the limited resources for the responsive management of change by developing countries, including many in ASEAN.

A. The new competition

Along with the challenges of competitive globalization and rapid technological progress have emerged vast, new opportunities for value creation and entrepreneurship. In addition, the scope and potential for new and innovative forms of industrial organization and management (including clustering and networking) have been greatly increased -- with the consequent and significant gains in collective efficiency, flexibility and hence competitive advantage by business enterprises within and across borders (Porter, 1998).

1. Rich opportunities

Initially, external trade had been facilitated through the imposition of wide-ranging measures for economic liberalization and policy deregulation in economies of all shades of ideology from the late 1970s. Subsequently, the trade flows in goods, services, finance, technologies, and ideas have been greatly boosted by more comprehensive multilateral agreements -- such as those embodied in the World Trade Organization (WTO), and in several plurilateral arrangements (e.g., NAFTA, EU, AFTA etc.).

Meanwhile, an added impetus to trade-based interaction has emanated from the rapid and cumulative advances in ICTs themselves (more below). For all practical purposes, therefore, all kinds of supplies and inputs can now be sourced from all corners of the world -- whether they are tangible or intangible, or in financial or physical forms. The process is mediated competitively, on a rules-based basis, and often in real time as well.

The upward trends in trade liberalization have resulted in the commercialization of a larger amount of global production. For example, the value of world trade (or world exports) reached US$ 12,665 (or US$ 6,178) billion even in the economic slow down of 2001; the corresponding figures for ASEAN trade being some US$ 749 (US$ 399) billion.[19]

Meanwhile, the proportion of merchandise exports to global output stood around 12 per cent in the early 1980s; it almost doubled to 20 per cent in the early 2000s. Strikingly, the relative share of manufactured exports jumped from 28 per cent in 1975 to an estimated level of over 85 per cent in the late 2000s.[20]

2. Complex obligations

But the almost unlimited opportunities for gainful growth through trade on the demand side are counter balanced by the equally numerous, and highly formidable, challenges to countries and corporations on the supply side. Some major challenges and issues have to be noted, selectively and briefly, as another backdrop for the policy measures and options to be suggested in Chapter Six of this blueprint.

One, WTO embodies the most ambitious and comprehensive architecture on trade ever designed, negotiated and agreed on multilaterally.[21] The consequent trade regime is

[19] 2001 was a year of world slowdown in economic and trade activities. The value of global and ASEAN trade was considerably higher in 2000, reaching respectively US$ 13,486 (US$ 6,873) and US$ 782 (US$ 421).

[20] See Lam (2000: 7-21) for more details on the main characteristics of the current wave of globalization – in terms of trade and capital flows, labour movements, production technologies, and new forms of industrial organization and co-operation.

[21] It covers all articles of GATT 1994 (as modified by the Uruguay Round); the Marrakesh Protocol to the General Agreement; the 12 constituent Agreements in the Multilateral Agreement on Trade in Goods (on Agriculture; on the Application of Sanitary and Phytosanitary Measures (SPS); on Textiles and Clothing; on Technical Barriers to Trade; on Trade-Related Investment Measures (TRIMs), on the Implementation of (respectively) Article VI (anti-dumping) and Article VII (customs valuation) of GATT 1994, on Pre-shipment Inspection, on Rules of Origin, on Import Licensing procedures, on Subsidies and Countervailing Measures, and on Safeguards); the General Agreement on Trade in Services (GATS); the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS); the Understanding on Rules and Procedures Governing the Settlement of Disputes; plus the four Plurilateral Trade Agreements (on Trade in Civil Aircraft, on Government Procurement, on International Diary, and on International Bovine Meat).

very complex. In addition, its wide-ranging ramifications are yet to be fully understood by interdependent countries and corporations alike, those in the developing world in particular.

Before 1995, developing countries were in effect exempt from most of the disciplines imposed on the contracting parties to GATT. They were accorded trade preferences (the Generalized System of Preferences or GSP) which were mostly non-reciprocal. In addition, the most favoured nation (MFN) treatment allowed them to benefit from the successive reductions in trade barriers negotiated among, and spearheaded largely by, the industrial countries.

However, provisions for special and differential treatment (S&D) under various WTO agreements have rendered such preferential treatment much more specific, and much less extensive and inclusive. At the same time, developing economies and, in many cases even the least developed among them, are assuming substantial new obligations in many new areas of the current trade rules.[22]

Meanwhile, there has emerged a plethora of trade issues and implementation problems with a recurring impact and implications on the enterprise sector, including SMEs.[23] Many of these issues and problems are likely to remain an irritant in trade relationships and in commercial diplomacy for some time to come, notwithstanding the current Doha (Millennium) Development Round of WTO launched in November 2001 (see Box IV-2 below).

[22] Outstanding issues in S&D treatment, including those related to implementation and technical assistance, are discussed in more detail in UNCTAD (2002: 42-45) and (1988a: 65-87); WTO (2002: 30-37), and Weston (1995: 64-85).

[23] There is now a "mountainous" volume of literature and research papers on the above matters (surf, for example, www.cid.harvard.edu/cidtrade/issuemain.htm). For a concise survey of some of the WTO-related issues, problems and policy options for the Asian least developed countries and economies in transition, see Lam and Wattanapruttipaisan (2001: 7-30) and the references cited therein. WTO (2002) provides birds-eye-view information on the current state of play in global trade, and Hoekman, English and Mattoo (2002) contains a collection of useful materials on multilateral trade-cum-development issues and options facing developing countries.

Box IV-2. Bird-eye's View of WTO Implementation Problems

There are many implementation issues and difficulties. One is the persistence in the trade regimes among the developed countries of significant tariff peaks and tariff escalation. These apply mostly on processed imports and, to a lesser extent, on competing imports from developing countries.

Two, the planned liberalization in textiles and clothing (to be completed by end-2004) has not led to a significant removal of quota barriers. This is largely due to "end loading" and "back loading" of the stipulated adjustments. Meanwhile, the additional market access in textiles and clothing so gained by developing countries has been somewhat offset by transitional safeguards and restrictive rules of origin.

Three, both developed and, to a lesser extent, developing countries have increased their reliance on anti-dumping actions and countervailing duties. Orderly and speedy dispute settlements are thus a prerequisite. Yet, the WTO dispute settlement model is far from ideal. It tends to be "lawyer-intensive", overly legalistic, and hence prohibitively expensive in terms of time and cost for most developing countries.

Four, standards, technical regulations, and SPS measures have proliferated at the expense of exports or potential exports from developing economies. Many of these trade constraining actions are of an opaque scientific nature, however.

S&D provisions in favour of developing countries in various agreements have proved, in practice, to be generally inadequate as regards, for example, the time required to complete the transitional adjustment and restructuring processes. In addition, they do not sufficiently reflect individual performance or the special needs of the intended beneficiaries (developing economies and LDCs).

All these issues are being addressed in the current Doha (Millennium) Development Round. Their complexity and intractability are evidenced by the extended deadline for reaching a consensus on strengthening S&D provisions to the end of 2002 (instead of 31 July 2002 as originally scheduled). It is likely that the extended deadline is going to be missed again, given the slow progress in current negotiations in Geneva.

Lastly, deep fissures persist on matters relating to certain aspects of international labour standards, trade and environment linkages, TRIPS, and the so-called four Singapore issues (trade and investment, trade and competition policy, transparency in government procurement, and trade facilitation). These problems are then compounded by the sharp differences in perceptions and expectations on a wide range of issues for negotiation among member countries.

As a result, the Third Ministerial Conference of WTO, held in Seattle in November 1999, failed to come up with an agreed agenda for the millennium round (successfully held in Doha in late 2001).

Likewise, integration efforts within ASEAN will open up significant new opportunities for trade in goods and in selected services sectors (e.g., "open-skies" air transportation, telecommunications, financial services, and FDI). In this connection, AFTA is perhaps most notable and more widely known.[24]

[24] The deadline for tariff reduction by the older six members of ASEAN has been repeatedly brought forward from the original 15-year period (starting from 1993) to the beginning of 2002, although with some flexibility. Of the newer members, Viet Nam is expected to realize AFTA by 2006, Lao PDR and Myanmar by 2008, and

The scheme has contributed to a faster rate of growth in intra-ASEAN trade, averaging 11.6 per cent annually between 1993 and 2000; intra-regional exports being some 23 per cent of total export value in 2000. These were higher than the annual expansion in ASEAN total trade as well as the amount of intra-ASEAN exports a decade ago. However, the 1997-1998 crisis obscured the picture somewhat; and so will the 2001-2002 global and regional economic slowdown.

Meanwhile, ASEAN integration efforts have also brought about formidable challenges to business entities, both large corporations and SMEs. Cursory evidence indicates that, just as in the case of WTO, the ramifications of these integration efforts across sectors and industries within ASEAN have yet to be fully understood. High-quality information and capacity-building toolkits are not adequately disseminated to all those concerned stakeholders in the region.

The tasks involved are clearly daunting. One, existing policies have to be re-orientated while new ones put in place across sectors and industries. Two, the necessary changes have to be made in laws and regulations, sector- and economy-wide. Three, the ancillary and complementary institutional and administrative infrastructure must be put in place, in addition to the many adjustments to be made to those already in existence, at various levels and layers of government

At the same time, measures have to be devised to assist and facilitate the pending tasks of defensive as well as positive restructuring of domestic sectors and industries. Necessarily, the process has to be based on perceived opportunities and shifts in comparative and competitive advantage in relation to domestic requirements and capabilities (both current and latent) within and outside ASEAN.

Thus, significant resources are required to minimize more effectively and speedily the inevitable economic disruptions and losses associated with the new trade obligations. This applies, in particular, to the maintenance of social security and the provision of social safety nets. But substantial resources are also needed to build up or re-establish local supply capabilities and competitiveness for gainful and sustained participation in the global and regional trading systems.

Generally, the process of adjustment and restructuring has proved to be highly complex, greatly sensitive, substantially time consuming and very costly. This has been amply revealed from the long (and often tortuous) experiences in the implementation of a variety of preferential trade areas (PTAs), free trade agreements (FTAs), and multilateral trade accords across the globe.[25]

Cambodia by 2010. Thus, from 2002, some 96.2 per cent of the products on the inclusion list will have tariff rates within the range of 0-5 per cent; tariffs on the remainder will fall within this range by the beginning of 2003. Currently, the average tariff rate on all goods traded within AFTA is about 3.8 per cent. In addition, the phase-in tariff reductions on items under the temporary exclusion and sensitive lists are expected to be completed by 2010 and 2015 respectively for the two groups of ASEAN members.

[25] For a detailed discussion on PTAs and FTAs, and on related policy issues and implications on economic statesmanship and political will among all concerned, see Asian Development Bank (2002: 157-196), Pomfret (2002), and WTO (1995:.25-62). Further references on the above subject matters can be found in the extensive bibliography contained in the first two pieces of work.

ASEAN regional and subregional cooperation and facilitation will certainly save much time and costs in the concerned processes. However, it is not in the scope of this proposed policy blueprint to discuss even a minimalist agenda, and related policy issues and implications, in trade- plus investment-based integration. On the other hand, those directly concerning the SME sector, plus remedial measures in capacity building and upgrading, are considered in this and the next two chapters.

3. Demanding markets

Consumer preferences and market demands pose the second set of challenges, as noted briefly earlier. On the one hand, they are constantly changing. This trend has been facilitated by the rapid advances in ICTs, bio-engineering, and new materials sciences. It has also resulted in new and innovative products and processes, and shorter product cycles and smaller output batches.

In particular, product quality and designs are generally much improved along with more frequent and innovative design changes, greater mass customization and more flexible specialization. Just-in-time sourcing and minimum inventory levels have become an important element in efficiency and competitiveness. This is achieved via, among other means, increasingly exacting timeliness and punctuality in delivery.

On the other hand, non-price parameters have become important determinants of competitive advantage. They include quality, health and safety, social equity in employment and production, and ecological implications of products and processes.

In particular, there is little room for compromise on quality (more in Chapter Five). Certification under the International Organization for Standardization (ISO) 9000 series of standards implies compliance to quality management systems recognized worldwide.[26] In addition, ISO 14000, focusing on environment safety and control, has gain much importance since the early 1990s.

The certification process helps to minimize waste and costs while maintaining or improving quality uniformity. Systematically, they ensure that the correct steps and operations are carried out or performed at the right time or right stage within the enterprise.

The certification and post-certification compliance processes can be both complex and time consuming, however. As such, they can be done in progressive stages.[27] This is well suited to the self-diagnostic and self-improving (toolkit-based) approach which will be examined at length in Chapters Five and Six.

But mindset changes are also required in other business practices not traditionally practiced or expected by most SMEs (Momoya, 2000: 160-161; and Altenburg, 1999: 32-34).

[26] See Minoza-Gatchalian (2001: 225-230) and International Trade Centre (1996: 3-27) for some pertinent discussion quality matters, and related issues and implications for SMEs.

[27] Ranging from quality awareness, conformance to specifications to ISO compatibility through total quality control, assurance and management. Firm-level performance at the last stages is benchmarked in terms of quality, cost and delivery (QCD); these parameters are also known as the three Ps – performance, price and punctuality. Conformance to QCD (or PPP) guidelines is among the prerequisites for NIP subcontracting and supply-chain-related outsourcing.

The new business perceptions and operational actions are discussed in more detail in Chapter Five.

4. Fiercer competition

Competition has become greatly intensified among the global and regional players and actors, SMEs included. There is also a much larger number of suppliers and providers competing for both existing and new markets for goods, services, finance, and other wealth-creating technologies and knowledge.

In particular, China is a huge potential market (including for ASEAN producers) of some 1.3 billion persons. In 2001, its GDP stood at around US$ 1,180 billion, compared to just under US$ 574 billion for ASEAN as a whole. Its trade turnover amounted to US$ 575 billion in the same year, compared to US$ 749 billion for ASEAN.

China has become highly competitive even before it became a WTO member in December 2001 (see Box IV-3 below).[28] It had been negotiating for GATT/WTO membership since 1986. In the intervening period, China has become the world's seventh largest trading country -- accounting for 4 per cent of global export value, and 3.5 per cent of world imports (UNCTAD, 2002: 141).[29]

[28] For further details, see OECD (2002: 138-142). Wattanaprutipaisan (2002b) provides a detailed analysis of the gains, issues and implications associated with the proposed ASEAN-China FTA; this proposal was made at the summit of leaders in Singapore in November 2000.

[29] In addition, China is the world's largest destination for FDI among the developing countries, hosting an inflow of US$ 47 billion in 2001. It is worth noting the growing attraction of China as the host economy for FDI. Such inward investment averaged just under US$ 14 billion a year during 1989-1994. The flow reached almost US$ 41 billion a year over 1995-2000. Some 400 of the Fortune 500 biggest corporations have investments in some 2000 projects in China.

Box IV-3. China: The Emerging Giant

Many producers in South Asia and South-East Asia, including several in ASEAN (both new and old members) have felt market penetration and displacing pressures from China. This applies, in particular, to those suppliers (especially SMEs) at lower stages of technology sophistication and with a high content of imported inputs. The products concerned include many lines of textiles and clothing, footwear, toys and plastic products, consumer electronics etc.

In addition, China also has a competitive edge or has developed competitiveness in a wide range of other manufactures. Among these items are building materials, machinery and electrical appliances, optical instruments, clocks and watches, measuring and checking instruments, metal products and chemicals.

In fact, such manufactured goods accounted for about 70 per cent of all ASEAN imports from China -- with machinery and electrical appliances alone amounting to just over one-half of total import value in 1999. They have also expanded faster than ASEAN import of similar products from all other sources during 1993-1999 (ASEAN, 2001).

Furthermore, China has managed with notable success to gain a larger foothold in the United States, the EU and Japan; these are, by far, the three most important export markets for both ASEAN members and China. The most pertinent case in point is provided by data from the G-7 market – consisting of Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States.

China's share in clothing doubled to around 20 per cent in the 1990s; such market gain has occurred largely at the expense of exporters from the Asian NIEs; however, the share of ASEAN-4 (Indonesia, Malaysia, Philippines and Thailand) remained largely stagnant at around 8 per cent in the same period.

The G-7 market for footwear is now dominated by China whose relative share was less than 10 per cent in the late 1980s but went as high as 38 per cent in the late 1990s. Again, this has taken place at the expense of both the Asian NIEs and ASEAN-4.

Similar trends in market penetration by China can also be observed in sectors such as telecommunications equipment, office and automatic data processing machinery, and electrical appliances. Meanwhile, China has been and will remain the dominant supplier of textiles and clothing to Japan, with a relative share rising from 44 to 62 per cent between 1993 and 1999.

B. The new technologies

ICTs, transportation and biological technologies, and the new materials sciences have shown rapid and self-reinforcing advances. Such progress has constituted another critical impulse for growth and transformation of enterprises, industries and economies, world-wide and regionally.

In particular, there has been an extensive and deepening penetration of innovative technologies and new materials in virtually all fields of human endeavours ranging from medical sciences to military applications. Such a widespread adoption and absorption, in

turn, have pushed up significantly the productivity, resilience, and flexibility of economic activities and services.[30]

1. Linkage facilitation

Firstly, connection to the World Wide Web has made access to global market, information and knowledge readily available in a relatively easy, generally inexpensive and virtually instant manner. As such, the new ICTs the key to opening the store of global ideas and technologies; these wealth-creating resources are not only bottomless but also constantly expanding, too.

Knowledge and learning capabilities have become, in their own right, a major determinant of economic efficiency, factor productivity, domestic and external competitiveness, and hence of business success or failure itself. This is true for all firms -- regardless of whether these enterprises are big or small, operate in manufacturing or in the provision of services, or are outward oriented or cater largely to the domestic market.

a. Clustering and networking of firms

Secondly, the ICT revolution has broken the tyranny of time and space. In the process, it has greatly facilitated inter-firm linkages and networking across political, ethnic and geographical divides. Traditionally, such inter-firm connectivity has been motivated by considerations of lean stocking, quality consistency, and just-in-time production and delivery (Meyer-Stamer, 1995: 143-146).

However, the ICT revolution (coupled with trade liberalization) has contributed to a paradigm shift in industrial organization itself. There is an on-going move from large-scale vertical integration of hierarchies (of the Fordish and Taylorish varieties) to flatter horizontal production arrangements. This is manifested in the multiplying networks and, to a much lesser extent, clusters of firms (see Box IV-4 below).

[30] UNCTAD (2001: 27-28). Largely as a result, the trajectories economic growth of many countries have been boosted higher and their competitive edge, become increasingly sharper. The United States economy, in particular, displayed an astounding performance in the 1990s with an extended period of economic growth which became the longest on record in April 2000. Equally striking is that yearly output expanded by some 4.0 per cent in America during 1997-1999, and by around 5 per cent for the first half of 2000. After a temporary downturn, U.S. productivity growth was in the range of 3-5 per cent a year in 2002.

Box IV-4. Alternative Modalities in Industrial Organization

In one form or another, clusters and networks of enterprises have had a very long history. There has been, however, a renewed focus on these alternative organizational modes in the last two decades.

The renew attention is due, in part, to basic advances in ICTs and transportation technologies, along with global trade liberalization. In turn, these development trends have greatly facilitated, as well as necessitated, the search for ways and means to maximize business efficiency and competitiveness.

Clustering of firms

Narrowly, a cluster of firms is a group of businesses which operate in a co-operative or competitive manner. These enterprises are normally congregate in a specific location and produce goods and services for the same industry or sector. Such an agglomeration of businesses also tends to be culturally homogeneous (Boari, 2001, p.2).

A broader definition views a cluster of firms as a group of inter-connected enterprises and associated institutions (e.g., universities, vocational training institutions, R&D facilities, standards-setting agencies, BDS providers etc.). These entities are found in a geographically "proximate" location. They are also linked by commonalities and complementarities which are important to competition and competitiveness (Porter, 1998, p. 78).

The broader view of clustering encompasses, therefore, businesses and institutions that cut across sectors and industries. Such heterogeneous and encompassing clusters include multi-media cities, growth metropolis etc., which provide more opportunities for cross-fertilization and hence collective gains, especially in innovation.

Logically, the broader definition of clustering also covers firms operating in neighboring countries as well. Thus, the distinction between clustering and networking is thus becoming less clear-cut. In particular, subregional growth areas (such as triangles or corridors or quadrangles etc.) can be broadly looked at as (spatially) clustered enterprises.

Networking of enterprises

Inter-firm networks exist both within and across borders. They, too, have had a long history. Such linkages involve interactions between enterprises, whether or not the pertinent relationships are on an arms-length basis or driven by equity stakes.

More recently, however, networking is often used to describe cross-border production and distribution arrangements. It thus denotes inter-firms interactions which cut across the value chain as well as national borders or geographical divides.

Generally, production and service activities are divided into smaller and more discrete functions to be performed by various participating nodes or connecting links within the production networks or supply chain concerned. These functions are then located and relocated, or sourced and out-sourced on the basis of several considerations.

One is to ensure that inputs and supplies for the networks or chains can be obtained most competitively and timely. Two is to help improve or upgrade their own access to resources, capabilities, knowledge and skills, and innovations. Three is to facilitate a more cost-effective and sustainable penetration by these

networks and chains in important and growing markets, market segments, and market niches.

Significantly, networks-based or chains-related subcontracting and outsourcing arrangements now cover a wide spectrum of activities and services of high value-addition and technological sophistication. These range from original equipment manufacturing, complete-package production, product design and engineering, R&D, to various other high-end support services.

b. Some advantages and disadvantages

Other things being equal, enterprise clusters and networks can be a dynamic force in development and modernization in localities both within and across borders. The proliferation of NIP and cross-border supply chains is an illustrative case in point (see Box IV-4 above). In particular, these NIP and chains have shaped and reshaped the industrial landscapes and industrial integration in Asia, among other developing regions.[31]

In particular, trust and confidence are two indispensable ingredients in any lasting relationships between or among firms. A significant, positive externality from the clustering and networking of firms is the gradual building up of these two critical parameters in the process.

Another positive externality is the specific or potential weaknesses and constraints in policy, institutional and support structures that the formation of inter-firm linkages and enterprise clusters can reveal for remedial purposes. This applies especially to the adequacy, or otherwise, of a variety of public (physical) infrastructure, financial facilities, training and research activities and so on.

Other the mutual gains are shared risks in product development and commercialization, cost spreading in (localized) infrastructure investment and R&D.[32] In addition, productivity is enhanced and cost reduced through economies of scale and scope, and better access to input (such as labour, technologies, transport services, and finance) and final markets.

Meanwhile, partnerships and collaboration among firms from different sectors or industries can be especially important in high-value, high-end markets. At the same time, such "dis-embodied" form of vertical integration also facilitates and induces a greater focus on the individual firm's own "core competence" along with the outsourcing of non-core tasks to other enterprises within the network or cluster.

Moreover, customers as well as of business associations and trade unions can greatly facilitate the clustering of firms, and inter-firm networking within and across border. They

[31] Borrus, Ernst and Haggard (2000) contains a collection of articles which deal extensively with international production networks in the Asian electronics industry. See, in particular, Borrus (2000: 57-79), Ernst (2000: 110-140), and Ernst and Ravenhill (2000: 226-256) plus the extensive references cited in these articles.

[32] Strategic alliances and other technological partnerships in corporate R&D have long existed among TNCs as well as between them and their local affiliates and non-affiliated companies. Such linkages normally involve large firms in developed countries and, to a much lesser extent, high-income developing economies. See UNCTAD (1999: 195-228) for a detailed presentation on the rationale and experiences relating to the above matters.

can provide as well a variety of feedback (of a backward, lateral and forward nature) which can help to increase the efficiency, flexibility and competitiveness of clustered or networked enterprises.

The above benefits are generally more important in demand-driven clusters and networks. But there are also instances of counter-productive competition thus contributing to a further erosion of profit margins through higher bidding costs for input supplies (such as skilled labour) and lowered prices for delivered products.

In addition, the concentration of physical business operations tends to impact negatively on (limited) infrastructure, especially on (current) congestion and environmental fragility. Another problem is that the vitality of clusters and (spatially local) networks has to be sustained over time with the on-going entry of new firms and industries for additional dynamism and efficiency (e.g., new technologies in process and quality control, innovative products and services etc.).

The collective benefits may fall off in stagnant (or dormant) and older clusters and networks. But new entry of firms in complementary industries or sectors also creates additional pressures on the current carrying capacity of infrastructure and the environment.

Generally, the experiences in promoting enterprise clustering and networking have been mixed in many developing countries, including those in ASEAN. This applies especially to efforts to involve SMEs as the main driving force or stakeholders the formation process. The main constraints in SME participation, and their policy implications plus remedial possibilities, are examined further in Chapters Five and Six of the proposed blueprint.

2. Cyber business transactions

ICTs have also reduced significantly business transaction costs. Their penetration is also particularly manifest in a wide range of service sectors, not least in the area of financial services (APEC, 2001; and UNCTAD, 2001). Most notably, the new technologies have fuelled the relentless upsurge of global e-commerce whose potential in terms of growth and diversification is simply tremendous

The e-market itself, estimated to be worth several hundred billions U.S. dollars in 2000, is expected to grow at an exponential rate to reach the trillion-dollar mark well within this decade.[33] Meanwhile, trade via the Internet has become an intrinsic part of an increasingly large number of SMEs in developed countries.

In particular, some one-half and one-third respectively of the medium and small-sized companies in Europe maintain an e-mail contact address or www presence. The number of internet hosts, for example, went up from just under 6 million connected servers in 1995 to some 37 million in 1998.

[33] It should be noted that there are presently very large variations in estimates of the size of e-commerce ranging, for example, from US$ 200 to over US$ 600 in 2000 alone. Such large discrepancies are due to definitional problems coupled with a critical lack of data and information. See APEC (2001) and UNCTAD (2001) for a comprehensive survey and useful analysis of issues relating to e-commerce; the latter with special reference to selected service sectors.

A word of caution is necessary, however. Firstly, the expansion of digital connectivity and e-trade has been highly uneven; geographically, the concentration is in North America and Western Europe. These regions, for example, accounted for 85 per cent of the value of e-transactions between businesses (or B2B) which were, estimated at around US$ 450 billion in 2001 (UNCTAD, 2001: 71).

Secondly, the conditions and circumstances of most SMEs in Asia and, for that matter, within ASEAN are vastly different from those of their counterparts in the developed regions.[34] However, the issues here are not whether but how best to assist SMEs to make the best use of ICTs for e-commerce and inter-firm linkages. These issues and their policy implications are discussed at length in Chapters Five and Six.

II. The imperatives of competitiveness

The new development context has moulded and shaped in a profound way the inter-relationships among various strata of interdependent players and actors within and across continents, economies and corporations. Its principal characteristics are encapsulated in Box IV-5 below for ease of consideration in relation to the wide-ranging measures and options proposed Chapter Six of the policy blueprint.

A. Learning-based competitive advantage

The traditional distinction between "standard" and "high" technologies is now much less illustrative or pertinent. Even labour-intensive operations under mature technologies (e.g., clothing, auto-parts production, consumer electronics manufactures etc.) still involve modern, computer-controlled machinery and other complex equipment. Thus, efficient and effective operations and maintenance depends much on the availability of knowledge-intensive skills and steps.

Complicated organizational arrangements and managerial expertise are another feature of modern businesses, whether these be large corporations or SMEs, (more in Chapter Five). There is, in addition, much systemic interactivity in terms of inter-firm linkages and international collaboration across the value-chain -- from input sourcing, production, product development, storage and transport, to marketing and distribution.

Likewise, productivity and competitiveness resolve around entrepreneurship, flexible specialization, and new and innovative products and processes (Chapter Five). These integral elements of core competence of an enterprise, in turn, are largely based on and driven by its capabilities in cumulative learning and un-learning (such as in knowledge-based innovation), and in inter-firm linkages and inter-agency networking (for collective gains in efficiency and flexibility).

B. Mobile and networked assets

[34] PricewaterhouseCoopers (1999) contains a useful survey of the main issues and constraints, both hard and soft in nature, relating to e-commerce and SMEs in the APEC region. A detailed consideration of e-commerce and low-income countries and economies in transition, specifically China, can be found in UNCTAD (2001: 189-250).

There is now an intense competition for such footloose resources (whether financial or human) at the global and regional levels. This means that, firstly, such assets are now even more selective in terms of their destinations and more volatile as regards their flow. Sustained capacity building (both skills formation and infrastructure development) and a judicious policy environment will provide an important edge in competing for and/or in retaining these wealth-creating resources.

Box IV-5. Parameters of the New Economy and the New Competition

One, economic efficiency, flexibility and competitiveness are increasingly human-made. Location, natural bounties, economies of scale, and hence size are important determinants of initial comparative advantage. However, they are no longer sufficient to ensure durable competitiveness in the long run.

Two, external wealth-creating assets and capacities include entrepreneurship, human and financial resources, technologies, and business alliances and partnering. All these can be attracted by, substituted for, and withdrawn from most economies, sectors and enterprises with relative ease and often in real time as well.

Three, an enabling policy environment is a prerequisite for greater as well as more gainful participation in economic activities by private entrepreneurs and enterprises -- large, medium, small and micro. A synergic partnership between government and the private sector, including for SME development and integration, is a prerequisite. And so is the maintenance of policy consistency, coherence and transparency within across sectors and industries.

Secondly, the knowledge and entrepreneurship base itself can be enlarged through a durable participation in multiple and diversified networks of collaboration within and across-borders. The interactive linkages can be backward (with suppliers) forward (with clients and financial or capital providers) or lateral (with science and technology infrastructure, productivity and training centres etc.)

Thirdly, clusters and networks of inter-linked firms can be a feasible alternative to fill up the "hollow middle", a typical weakness in the industrial structure in most developing countries, including those in ASEAN (Chapter Three). There exist at present a sharp divide between large-scale, (vertically) integrated corporations and a multitude of largely independent, family-owned and operated SMEs.

As a transitional step, for example, the formation on-line of a (formal or temporary) partnership, network or alliance of entrepreneurs or SMEs can appear as a single, diversified business to their customers or suppliers. Such inter-firm linkages, moreover, can respond more timely and flexibly to the snowballing opportunities and formidable challenges of the electronic market place.

C. A level playing field

Government has become "leaner and meaner" along with the process of liberalization, privatization and deregulation (Chapter Two). The public sector on its own is, by and large, no longer a force sufficiently potent and flexible to cope effectively and timely with growth and change.

Another issue is that government agencies responsible for R&D, BDS and extension activities are not often viewed by SMEs as important sources of support and development to them. On the other hand, the provision of BDS from the private sector tends to be problematic in terms of scope, regional coverage and affordability. This is particularly true among middle- and low-income economies, and those in market-based transition**.**

Thus, a level domestic playing field also requires a synergic partnership between government and private enterprise in support of SME development. This implies, firstly, the availability of well-established, clear-cut and predictable guidelines and benchmarks for joint efforts; the principle of subsidiarity is pertinent in this connection (more in Chapter Five).

Secondly, closer interactions and more frequent dialogues are also needed at various levels and layers of the public and private sectors to ensure, among other things, that SMEs are effectively "crowded" into the policy framework.[35] Effective representation from the SME sector in such a process is of critical importance. So is the ways by which such interactions and dialogues are mediated and coordinated institutionally (more in Chapter Five).

[35] In many developing countries, most ASEAN member countries included, macroeconomic levers often do not connect or connect loosely to all the underlying sectors, enterprises, and entrepreneurs. This is due, in part, to persistent bottlenecks and acute shortages in soft and hard social, economic and other infrastructure. These constraints have weakened considerably the intended impact of policy leverages and inducements on the expected behaviors of the targeted groups or economic units, specific segments of SMEs included.

Chapter Five

CONSTRAINTS ON SME DEVELOPMENT IN ASEAN

Contents

The current state of SME development and integration is unsatisfactory and, in many instances, worrying in most parts of ASEAN (Chapter Three). Major problems and constraints facing SMEs have been well known for quite a long time.[36] They will not be repeated in the following chapter in any detail -- except where these problems and constraints are directly specific to the policy approaches, measures and options being suggested in Chapter Six of the proposed blueprint.

[36] There is a very large volume of literature on the wide-ranging and typical constraints and difficulties facing most SMEs. See, for example, Freeman (2002); Tan (2002); Urata (2002 and 2000); Alfonso and Co (2001); Regnier (2000); Tambunan (2000); UNCTAD (2000); Lam (1999); ASEAN Secretariat (1998); van Diermen *et al.* (1998); APEC (1997); Pangestu (1996); Ng, Freeman and Huynh (1996); Hill (1995); and APEC (1994a and 1994b).

I. Sustained entrepreneurship development

It is now almost universally recognized that entrepreneurship is the foundation of gainful progress under the market economic system. Entrepreneurs often are not the same as manager who normally take charge of the operational aspects of a business. Both, however, will have to adapt and evolve along with the growing volume, sophistication and diversification of economic activities and services under the new economy and the new competition (as discussed in Chapter Four).

A. Context and constraints

Entrepreneurs are agents of innovative change because of their ability to identify and respond swiftly to potential or new opportunities in business, or in innovation or invention for commercialization purposes. Such a response, in turn, determines how well their own enterprises and, more generally, their own industries and the overall economy will perform and compete (see Box V-1 below).

Box V.1. Characteristics of an Entrepreneur

Date	*Author(s)*	*Characteristics*
1730	*Cantillon*	*A self-employed person with uncertain returns*
1767	*Nicollas*	*A leader of men, a manager of resources, an innovator of ideas, including new scientific ideas, and a risk taker*
1803	*Say*	*A coordinator of production with managerial talent*
1848	*Mill*	*Risk-bearing*
1917	*Weber*	*Source of formal authority*
1921	*Knight*	*A manager responsible for direction and control, who bears uncertainty*
1934	*Schumpeter*	*Innovation, creativity and initiative*
1954	*Sutton*	*Desire for responsibility*
1959	*Hartman*	*Source of formal authority*
1959	*Penrose*	*A person with managerial capabilities separate from entrepreneurial capabilities, and able to identify opportunities and develop enterprises*
1960	*Stepanek*	*A moderate risk-taker*
1961	*McClelland*	*Risk-taking and need for achievement*
1962	*Budner*	*A person with a high tolerance for ambiguity*
1963	*Davids*	*Ambition, desire for independence and responsibility, self-confidence*
1964	*Collins*	*A person with a high need for autonomy*
1964	*Pickle*	*Drive and mental force, inter-personal skills and communication ability, and technical knowledge*
1965	*Litzinger*	*Self-reliance and non-conformity, leadership, decisiveness, determination, perseverance and*

		integrity
1971	*Palmer*	*Risk measurement and management*
1971	*Hornaday and Abound*	*Need for achievement, autonomy, aggression power, recognition, innovative and independent*
1973	*Winter*	*Need for power*
1974	*Borland*	*Internal locus of control*
1974	*Liles*	*Need for achievement*
1977	*Gasse*	*Personal value orientation*
1978	*Timmons*	*Drive and self-confidence, goal-oriented, moderate risk-taker, locus of control, creativity and innovation*
1979	*Kirzner*	*An arbitrageur*
1980	*Sexton*	*Energetic and ambitious, positive in setbacks*
1981	*Welsh and White*	*Need to control, responsibility seeker, self-confidence and drive, challenge taker, and moderate- risk taker*
1982	*Dunkelberg and Cooper*	*Growth-, independence-, and craftsman-oriented*
1993	*Kao*	*Person who undertakes a wealth-creating activity and value-adding process through incubating ideas, assembling resources and making things happen*

Sources: Based on Timmons (1990: 163) and Tan (2002: 11)

In the above context, there is lack of an established and durable track record of sustained entrepreneurial drive in the SME sector of most ASEAN economies. Such a significant weakness is then compounded by an inadequate culture of innovation and (trust-based and confidence-driven) networking. This is well evident across a wide range of supportive activities and services – laterally, and both downstream and upstream as well.

Bottlenecks in entrepreneurship development are manifest among several high-growth "tiger" economies -- those in South-East Asia especially. This is attributable partly to their heavy reliance on the transfer, adaptation and dissemination of imported technologies in industry and management. Such dependence was a factor behind the controversy concerning TFP in the mid-1990s (see Box III-1 above).

It is likely these tiger economies cannot sustain their (exceptionally high) rates of export competitiveness and income expansion without a larger base of domestic entrepreneurship and technological capabilities. This consideration takes on special significance in view of the high levels of unemployment and disguised unemployment which have remained after the 1997-1998 crisis (Chapter Three). There is also a large pool of persons seeking to enter the workforce year after year.

But the incubation of a culture of entrepreneurship, innovation and networking has become even more essential under the new development context (examined at length in Chapter Four). Adequately empowered by sustained entrepreneurship, SMEs will enjoy an inherent comparative advantage in terms of their small scale of operations, and their greater

flexibility to adapt and respond to on-going changes in consumer preferences and market demands.

B. Current efforts and issues

Systematic programmes and projects are thus needed to identify potential entrepreneurs as well as to incubate a spirit of entrepreneurship particularly among SMEs, the young, the school leavers and new graduates. Yet, training in entrepreneurship development has not been pursued on a sustained basis. In addition, the promotion and incubation of a culture of entrepreneurship, innovation and networking has not been given on-going attention in most parts of ASEAN.

There have numerous training programmes in SME business and human resource development. Many are funded by both multilateral agencies (including the Asian Development Bank, the World Bank and UNDP) and bilateral donors, notably Japan. But most of these programmes are concentrated on the generation of specific skills in (formal) enterprise management, finance and marketing. Focus, targeting and outreach also pose difficult problems in their implementation process.

Besides, there is virtually no follow-up monitoring and assistance in remedial and additional training for the same group of SME beneficiaries. This has prevented the maximum utilization of the knowledge and capabilities gained by trainees, and hence of the overall utility and effectiveness of the concerned programmes.

Moreover, there is no emphasis on building up local capabilities for training in entrepreneurship development. Such capacity generation is the most cost-effective way to maximize outreach. It also facilitates a more widespread replication of the pertinent training activities within the domestic economy and, with appropriate certification, in neighboring countries as well.

The proposals for local capacity generation in entrepreneurship development to be made in Chapter Six are intended to overcome some of the above limitations and constraints. An additional advantage is their focus on SME capacity building in terms of the built-in training in business plan preparations and inter-firm networking. Moreover, these proposals are suitable for implementation and replication on both a regional and national basis.

II. Ancillary business capabilities

But entrepreneurship training is not the end of the story. Success in business also depends heavily on the availability and possession of a variety of skills, expertise and experiences in several other areas of enterprise organization and management.

A. Context and constraints

The prerequisites for efficiency, flexibility and competitiveness are not widely distributed even among SMEs in the top layers within priority sectors and industries. This has been another perennial bottleneck in SME sector development and integration in ASEAN, and elsewhere too.

In addition, the requisite skills in the organization and management of production and marketing have taken on modern shading because of competitive globalization and rapid technological advances. These impulses and imperatives for competitive change are creating new, innovative and dynamic modes and manners of production and service.

In particular, both big business conglomerates and SMEs are obliged to seek out the most efficient strategies for development and competition. Among other things, effective systems must be adopted for better quality and environmental control, cost and productivity improvements, and more flexible schedules of delivery timeliness.

Meanwhile, value creation can also come from new and innovative ways and means of industrial organization and co-operation in many fields of activities and services. This applies especially to concerted efforts made to obtain deeper knowledge of suppliers of the latest technologies, of competitors' behaviors and product plans, and of customers' needs and market demands.[37]

The basic business capabilities at the enterprise level are wide ranging. Some of them are selectively indicated in Box V-2 below for ease of further reference.

[37] The collection of several articles in volume one of UNCTAD (2000) contains a detailed analysis of issues in organization, management, production and marketing with special reference to SMEs.

Box V-2: Basic Capabilities at the Enterprise Level

Management of enterprise

- *Strategic planning*
- *Business planning*
- *Market analysis*
- *Accounting and book keeping*
- *Management of credit and working capital*
- *Negotiation skills*
- *Networking skills*
- *Personnel management*
- *HRD*
- *Skill development*
- *Information and documentation management*
- *ICT systems and planning*
- *Website management*

Management of production and marketing

- *Marketing*
- *Export marketing and documentation*
- *Package design and packaging*
- *Import sourcing and documentation*
- *Sourcing and storage of inputs*
- *Cost control and management*
- *Recycle and disposal of waste materials*
- *Work flows and production processes*
- *Technology upgrading*
- *Product design and differentiation*
- *Product testing and commercialization*
- *Maintenance and repairs*
- *Technology sourcing and upgrading*
- *Quality awareness and assurance*
- *Total quality control and management*
- *Improved input applications and substitution*
- *Safety improvement and accident prevention*
- *Environmental management*

B. Current efforts and issues

Enterprise capabilities and competitiveness can be built-up or acquired through the provision of BDS and extension activities from the public and private sectors. Such provision can be made at full or partial recovery of costs in cash and/or kind. Generally, however, the effectiveness and adequacy of BDS for SMEs have often been "problematic" in most parts of the developing world, including ASEAN.[38]

To begin with, the private supply of BDS and extension activities is not well developed, sufficiently diversified, and directly relevant and easily affordable. This is especially true in most ASEAN countries and not just in those economies where the private sector is weak.

Thus, until the situation has changed substantially, public-sector agencies will necessarily have to be the principal source of BDS and extension activities for domestic firm, SMEs included. However, public-sector BDS are generally not that flexible and adaptable to changing needs. They also tend to be managed and delivered largely on a bureaucratic manner, and on a supply-driven basis.

[38] Hurmerinta-Peltomaki and Nummela (2000) and other articles on the supply of non-financial BDS in volume two of UNCTAD (2000) provide a detailed examination of the pertinent issues and related policy implications and options.

Furthermore, the inherent lack of financial resources and skilled human resources means that public provision of BDS is unlikely to be adequate relative to needs. New and innovative modalities for the delivery of BDS and extension activities to SMEs are needed. As far as possible, the main objectives should be substantive relevance and extensive outreach. In addition, cost-efficiency and financial sustainability are other equally important considerations.

Joint public-private sector programmes and projects in the provision of BDS and extension activities in favour of SMEs are thus important in the above context. But SME capacity building and enhancement on a self-reliant and self-service basis is equally important although such an approach has been overlooked in many countries. All these considerations are embodied in several innovative proposals for SME capacity building in basic organizational and management skills to be made in Chapter Six.

III. Monitoring and benchmarking competitiveness

Learning what a country and its enterprises are, or can be, good at producing is a key challenge of economic development on the supply side (Rodrick, 2002: 7a). Building up the capabilities of its enterprises for durable compliance to market requirements and consumer prerequisites is a key challenge on the demand side.

The following discussion focuses on supply-side aspects of SME capabilities and competitiveness in production and marketing. The nature and implications (on SMEs'skill base) of demand-side preconditions and other requirements, those from NIP and supply chains particularly, are examined at some length in the next section. As noted earlier, these prerequisites are both numerous and increasingly exacting over time.

A. Context and constraints

Up-to-date and comparable data and information on the supply side are currently not available for all practical purposes. This applies especially to those needed to monitor, evaluate, compare and benchmark the evolving capabilities and competitive potential of SMEs, those on of the top layers in priority sectors and industries especially.

Such an acute shortage is another serious structural weakness in statistical service in most developing countries, including many within ASEAN; this has persisted despite the inherent importance of, and the recent refocus of policy attention on, the SME sector. The chronic shortage has also constrained policy design, targeting and implementation in several ways.

Box V-3: The Needs for SME Supply-side Databases

Firstly, serial data and information on SME capabilities and competitiveness are indispensable for an accurate identification of the current core competencies as well as shared areas of weakness (for follow-up capacity building) among various segments of the SME sector. Dynamically, they constitute a systematic and robust indicator of the on-going changes (whether progressive or regressive) in SME efficiency, flexibility and hence competitive edge over time.

Secondly, operational benchmarks and guidelines can be distilled from the available information and data on the supply side capabilities and

competitiveness of top-rank SME in priority industries and sectors. They provide thus a solid set of good or superior practices for emulation or replication by those SMEs presently in the lower ranks or tiers in terms of, for example, cost, price and delivery. Such a process can be largely on a self-reliant basis (noted earlier), or through access to BDS and extension activities.

Thirdly, better and more effective tracking and assessment of the impact of SME-related policies, programmes and projects are not possible or sustainable without such serial data and information on SME capabilities and competitiveness. Yet, these critical dimensions of performance management have been relatively neglected for quite some time (more in Chapter Seven).

Fourthly, the collected statistics and information will facilitate the gradual build-up of databases for multiple applications and utilization. These databases can be classified according to sectors, purposes (e.g., e-commerce, subcontracting, clustering and so on) or competitiveness benchmarks (for example as regards quality, cost and delivery etc.). They thus provide "historical" foot-prints of the performance and evolution of the SMEs concerned and, by extension, their own sectors or industries.

To be credible, the data and information for monitoring and benchmarking SME capabilities and competitiveness have to be obtained in an objective, systematic, periodic and (statistically) robust manner. In this connection, the following notes serve to illustrate the nature of as well as some of the main issues to be covered in such an exercise.

B. Current efforts and issues

Capabilities, just like a rich base of physical resource endowments, are not sufficient to guarantee present or to sustain future competitiveness (see Box V-4 below). There are deeper factors and forces at work in transforming capabilities into comparative and competitive advantage.[39]

[39] These including not least the availability of socio-cultural capital (such as work ethics, trust, moral norms, ethnic- or community-based networks etc.), the supply and affordability of economic and social infrastructure and services, the quality of domestic policies and institutions, the extent of development-oriented governance, a culture or tradition of entrepreneurship and innovation, research and development institutions and facilities, and the auspiciousness of external conditions and circumstances. Some of these components, in particular development-oriented governance, have posed contentious issues both before and after the publication of a study by the World Bank (1993) on the East Asian (economic) miracle.

Box V-4. Foundations of Competitiveness

Just as the case of acquired capabilities, competitiveness is not a static concept (Porter, Sachs and McArthur, 2001: 16-19). It is the result of learning, upgrading, differentiation and innovation for continuous productivity enhancement. Such a process is an integral part of the firm's efforts to adjust competitively to an environment of constant change but still of ever-fierce competition and rivalries.

The needs for on-going improvements are inevitable. Simple, initial price advantage will be exhausted or eroded over time by a variety of bottlenecks and pressures. Among these are the rising costs of labour and land, the widening infrastructure shortages, more intensifying competition, and the increasing fragmentation and sophistication of final markets.

In connection with these, learning and innovation play a key role in initiating sharpening and sustaining competitive advantage. These critical parameters of competitiveness can be further leveraged by inter-firm linkages, among other efforts at internationalization and re-engineering. Such efforts may range from mergers and acquisitions, being part of clusters and networks of collaborative firms, to the formation and deepening of specific (and time bound) strategic alliances and technology partnerships, as pointed out in Chapter Four.

Competitiveness has a foundation in microeconomics, whether or not it is measured and benchmarked at the industry, sectoral or national level (Meyer-Stamer, 1995: 143-146; and Porter, Sachs and McArthur, 2001: 21). In this context, the issues of, and the strategies for, promoting national competitiveness have attracted world-wide attention – especially from those in business, government and, to a lesser extent, the academia.

Among the most well-known cases in point are the current and growth competitiveness indices (or CCI and GCI respectively) as reported annually by the World Economic Forum (WEF). These indices cover 76-80 countries. Meanwhile, the world competitiveness index (with 49 countries in the sample) is compiled also yearly by the International Institute for Management Development (IMD). There are, in addition, several indicators of competitiveness at the regional level (such as Africa, Asia etc.).

Few exercises, however, have been carried out to measure, evaluate and benchmark the capabilities and competitiveness at the firm's and, to a lesser extent, at the domestic industry's level. This is true as far as published or publicly available publications and reports are concerned. Even much rarer are those periodically carried out for or on behalf of SMEs – for obvious reasons of the huge size, the acute shortage of information and data, and hence the substantial transaction costs involved.

Porter and his colleagues coordinate the WEP reports on CCI and GCI; the former had previously been labelled simply as the Competitiveness Index before the 2000 Report by WEF. As can be expected, the CCI is underpinned by Porter's celebrated diamond of competitiveness at the firm's level (1990).[40] This accounts for the strong emphasis on the

[40] This diamond consists of (the sophistication of supply) factor inputs and markets; (the demanding nature of) demand conditions; (the availability of innovative and complex) related or support industries; and (the presence of advanced and superior) corporate strategy, structure and rivalry. Government and chance (resource endowments) do have an impact and influence on various interactions among the four angles. Porter's diamond

importance of advanced business strategies and superior business coordination at the corporate level.

These two factors are regarded as the main determinants of the shifting patterns of corporate competitive advantage over time. However, they are more typical of firms operating in the OECD business environment. This milieu is far from similar to that in which SMEs are run in most parts of the developing world.

In addition, the business challenges to, and the perceptions of, OECD-type executives are certainly far different from those facing SME entrepreneurs in the developing region, including those within ASEAN. This applies especially as regards the penetration of ICTs and e-commerce, access to (domestic and external) credit and capital, technological infrastructure and facilities and so on (more in the several sections to follow).

In particular, SME technological capabilities are the main forces behind any discrete improvements in quality, cost and delivery; in turn, such on-going gains determine the competitive edge of the firm over time, as noted previously. But technological capabilities are a function of domestic infrastructure and facilities (both hard and soft) relating to R&D, education, training, BDS and extension activities.

The new development context has another inherent dimension, however. Matters relating to intellectual property (IP) and its protection have played a more significant role in the infrastructure and facilities, noted above, and hence in the process of acquiring technologies and technological capabilities, too (see Box V-5 below).

of competitiveness captures much of the dynamism and non-linear relationships and uncertainties of significance to business executives and management practitioners (Lall, 2001: 1510; and Momaya, 2001: 49-52 and 128).

Box V-5. The Growing Importance of Intellectual Property

To begin with, the TRIPS agreement of WTO embodies the extension of minimum standards for the protection of IP rights across the globe. Such a universal protection has also been increased in an unprecedented manner in terms of both level and scope.

Firstly, IP protection now covers the patenting of living things and materials found in nature, including geographical indications. The previous protection was accorded mostly to products and processes made by humans and inventors – such as patents, industrial designs, and trade secrets.

Secondly, IP protection regimes and regulations for literary and artistic property were mostly related to copyrights (more in point sixth). It is now modified to accommodate new technologies (especially those relating to biology and information processing and dissemination). Software sources and codes, and computer programmes are regarded as literary expressions for such protection purposes.

Thirdly, new technical areas and substantive fields are now under IP protection; these include software and business methods, and sui generis (of its own kind) regimes for semi-conductors, databases, plant (and animal) breeders' rights and so on.

Fourthly, a new emphasis is now given to the protection of new knowledge and technologies originating from the public sectors, including R&D and tertiary institutions. Thus, global access to publicly-funded research and its results may not remain unrestricted, as has been the case. Developed countries are by far the most overwhelming source of cutting edge research and technologies.

Fifthly, traditional knowledge folklore and genetic resources are under focal consideration for IP protection at present. Such knowledge includes tradition-based inventions and innovation which are specific to a certain location or people.

Sixthly, there is a widening of exclusive rights, an extension of the period of protection, and the strengthening of related enforcement mechanisms. In line with European practice, for example, copyrights are now extended from 28 years (renewable for another 28 years) to 70 years after the death of an author or 95 years from publication.

The new IP regime is a mixed blessing; again, new opportunities are being opened up for, along with difficult challenges being posed to, SMEs in their continuous efforts to enhance their own capabilities and hence competitiveness.

Notably, many of these opportunities and challenges are not confined solely to the legal and regulatory infrastructure and facilities for the registration, monitoring and enforcement of IP rights. They extend more generally to the patterns and processes of socio-economic and technological advancement as well. Yet, the impact and implications of the new IP regime are not well understood, particularly in most developing countries (see Box V-6 below).[41]

[41] A comprehensive survey and analysis of IP rights and economic development, with special reference to developing countries, can be found in a detailed report by the (United Kingdom) Commission on Intellectual Property Rights (CIPR) (2002). This handy and careful piece of work, consisting of a 176-page main report and a series of supporting documents of some 500 pages in length, should be a recommended reading for all persons interested in matters related to IP and development.

Box V-6. Intellectual Property Rights and Development

The presence as well as influence of ICTs is now felt across all fields of human endeavours. Similarly, IP-related matters and issues are exerting an increasingly profound impact on the nature and patterns of economic, social and technological development of developing countries.

Such an impact has not yet been well understood, especially as regards the available opportunities for better use of the rich and diversified local resource base in these countries. But it has important and multi-dimensional issues and implications for development policy.

These issues and implications concern, in particular, external trade, investment, the transfers and assimilation of external technologies. But they also influence the pace and patterns of local generation, adaptation and diffusion of modern technologies and technological capabilities.

Many of these issues and implications must be (but are not as yet) well appreciated by developing countries. This is necessary so that suitable responses in capacity building can be adopted across a wide range of socio-economic and technological areas.

Generally, there are sectors which are particularly sensitive to IP right protection (e.g., chemical, pharmaceutical, biological to name just a few). External trade and FDI inflows in these sectors may rise along with a strong IP protection regime.

Meanwhile, however, important segments of domestic sectors and industries may be deprived of reverse engineering opportunities (e.g., copying and imitation). In addition, high prices may have to be paid on imported consumer goods (including chemicals and pharmaceuticals), producer machinery and equipment, and technology licensing. The impact would be comparatively more severe on the poorer and lower-income developing economies.

Reverse engineering used to be an important springboard for acquired technological capabilities; these constitute the foundation for their later expansion. Reverse engineering activities also accounted for a sizable source of income and employment in several newly industrializing economies (NIEs).

IP protection was generally weak at the earlier stages of socio-economic development in these NIEs. This characteristic was nothing exceptional, however. The now advanced countries in the West also had a relatively weak regime of IP protection at the early stages of their industrialization.

In fact, they had long been able to tailor IP protection to suit their own condition and circumstances in development. This went on virtually unconstrained until the adoption in 1883 of the Paris Convention (on industrial property protection) and the 1886 Berne Convention (on the protection of literary and artistic works). In addition, their IP regimes did evolve in response to the changing impulses and imperatives associated with various stages of their own development.

It is not in the scope of this policy blueprint to examine the specific parameters and benchmarks in IP right protection most suitable to the specific development stages of various ASEAN members. It is pertinent to note at this juncture, however, that the monitoring, assessment and benchmarking of the evolving SME capabilities and competitiveness are long over due. It is imperative that the process be kick-started as a matter of pressing importance.

A detailed framework for such a remedial exercise is proposed in Chapter Six of the policy blueprint. Due attention is also given to IP-related matters in the framework. In addition, a pilot survey is also suggested to facilitate the related preparations and fine-tuning processes; these are inevitable in any sample survey of this nature.

IV. Fostering readiness for subcontracting

Both big corporations and SMEs are under tremendous pressures to innovate and change. These pressures are going to intensify greatly under the new development context (discussed at length in Chapter Four). The management of innovative change applies to the organizational and operating structures; to the degrees of focus on core competencies, including through inter-firm linkages and outsourcing; and to ensuring greater efficiency and timeliness in sourcing, production, marketing and delivery.

A. Context and constraints

Generally, enterprise clustering and networking can be a valuable bridgehead to domestic and external competitiveness.[42] In fact, the promotion of these alternative modalities of industrial organization and co-operation has been given a high policy priority in the developing world, including ASEAN.

However, success is mixed especially as regards to policy efforts to involve SMEs as a major driving force or stakeholder in the formation of clusters and networks.[43] This is, firstly, because of the lack of trust and an inward-looking attitude, particularly among SMEs which were founded and operated largely as family enterprises or family-owned businesses.

Secondly, the new modes of production and linkages require basic adjustments in business strategies, operations, technologies and, equally important, mindset. By and large, however, most SMEs often do not have the necessary resources, knowledge, and information to transform and to manage effectively the multi-faceted interactions in enterprise clustering and networking.

A related compounding factor is the lack of infrastructure and facilities for trust and confidence building under the auspices of government or of public-private sector collaboration.[44] Indeed, the limited evidence available shows that in a majority of clusters,

[42] Some of the main categories of advantages and disadvantages of clusters and networks were discussed in Chapter Four above.

[43] Indonesia has perhaps the largest number of enterprise clusters within ASEAN, a development attributable to its large economy and long tradition of concentration of cottage and household businesses. Some 12,000 out of nearly 70,000 villages were registered as industrial clusters in the country. About 5,600 of these clusters are found in Central Java (excluding Jakarta). For a variety of reasons, however, it appears that the large bulk of Indonesian clusters are dormant or have not been able to sustain the transformation into "dynamic" agglomeration of firms (Supratikno, 2002: 15; and Urata, 2000: 127-128).

[44] Among the trust- and confidence-building measures of a passive nature are information dissemination and the sharing of experiences; and involvement in public-private sector dialogues, trade fairs, study visits and

SMEs collaborate with one another only in a limited extent. Few firms specialize wholly on their on core competencies (Berry, Rodriguez and Sandee, 2002, pp. 370-371).

To a considerable degree, the prevailing constraints discussed above are less severe in demand-driven clusters. The active involvement of buyers and clients (whether or not they are TNCs or large domestic companies) brings to such clusters a range of complementary facilities and services. These include finance, material inputs, designs and appropriate technologies for backward services. Among the available forward services are packaging, advertisement and distribution, and marketing channels and market access.

Thus, demand-driven clusters resemble in several ways a collaborative node in the inter-linked production networks and supply chains, whether domestic or external. A supply-driven concentration of firms, on the other hand, depends heavily on close interactions across all stages of the value chain among the SMEs involved. As such, it is more vulnerable to many of the typical constraints borne by the SME sector.

However, there is some evidence that producer-driven clusters tend to have better prospects if engaged flexibly in small-batch production runs and/or in made-to-order supplies (mass customization). Part of the reason is their greater flexibility on the supply side, plus the availability of customer feedbacks for improved quality, cost and delivery. As a whole, further research is needed in the formation, deepening and expansion of geographical clusters of firms, including those within the ASEAN context (see Chapter Six).

B. Current efforts and issues

Some specific issues need to be highlighted in the context of inter-firm relationships and partnering. On the supply side, the virtually absence of solid and comparable information as regards the evolving capabilities and competitiveness of SMEs was discussed in the previous section. This constitutes, in turn, a major drawback in business matching policies, forums and trade promotion fairs as well as in the evaluation of their impact for remedial purposes (see Box V-7 below).

internship schemes. More active measures to foster trust and confidence include participation in risk and cost sharing schemes (e.g., in joint product development, testing and commercialisation; R&D, establishment of local or localized infrastructures and facilities etc.), collective quality and standard setting, joint negotiations for better access (to markets and for inputs), more effective representation to and improved interaction with government, and so on.

Box V-7. The Missing Links in Business-matching Activities

The yawning information gap has prevented a more business-like, systematic and objective way to carry out inter-firm matching and linkage activities. These have taken place in an ad hoc or haphazard manner so far because of the lack of (supply-side) history and data on the evolving capabilities and competitiveness (whether progressively or regressively) among the participating SMEs for comparison and cross-checking purposes.

To begin with, a product or service, which is exhibited or presented as a sample, may appear competitive on quality, cost and delivery considerations. There is no guarantee, however, that the production volume or variety of supplies can be increased by the pertinent SMEs in a cost effective and timely manner, and with their quality and reliability remaining uniform or assured.

In addition, sustained competitiveness depends on continuous, learning-based and innovation-driven improvements in product quality, cost and delivery. Again, however, the SMEs concerned may not be able to realize the required improvements and upgrading efficiently, and on an on-going and flexible basis.

The above weaknesses have been responsible, in a large part, for many unfavourable outcomes in business matching policies, forums and trade promotion fairs. In particular, there are the low rates of follow-up success relative to the initial one-on-one enthusiasm, or to the large number of signed memoranda of understanding on outsourcing and subcontracting.

Meanwhile, there is a specific issue on the demand side. Under the new development context (Chapter Four), the sustainability of inter-firm relationships and partnering is conditional on a durable compliance (by the participating suppliers and producers) to a large number of pre-specified, and increasingly exacting, requirements and expectations from their NIP buyers and supply chain procurers (Altenburg, 1999: Gereffi, 1999; and Humphrey, 1998).

The compliance process requires important changes in mind-set as well as in business practices themselves. In fact, many of the subcontracting prerequisites are traditionally not practiced or expected by most SMEs, among other firms, in developing economies. Specifically, for example, there is little room for compromise on quality or delivery, on constant efforts for productivity enhancement, and on the "social aspects" of working conditions and workers' amenities (Chapter Four).

As indicated in the previous section, the supply-side problem is to be redressed by new approach, suggested in Chapter Five, for the monitoring, evaluation and benchmarking SME capabilities and competitiveness on an objective, systematic and (statistically) robust manner. The demand side issue, as discussed above, is to be resolved through another innovative approach which is also proposed in the same chapter. This concerns the monitoring and certification of SME readiness to participate as subcontractors in NIP or supply chains.

V. ICTs and e-commerce

The development of ICT infrastructure, facilities and services is part and parcel of the domestic process of socio-economic advancement and structural transformation in the long term. As such, the overall national objective, strategy and policy have to be geared toward a

more effective and sustainable diffusion and adaptation of ICTs economy-wide, and not just in the business sector alone. This applies especially in the context of low- and middle-income countries where access to, and the availability of, ICTs tend to be limited.

A. Context and constraints

By nature, the process of ICT development has substantial requirements on resources. It also has wider and far more complex implications across many domestic sectors, both economic and non-economic. These include electricity generation and transmission, education and training, hardware and software developments, ownership and participation by different socio-economic strata and stakeholders etc.[45]

Thus, ICT matters cannot be adequately discussed on their own, or with reference only to one of ICT-based applications, namely e-commerce. Given this qualification, the major constraints on SMEs as regards ICT and e-trade penetration can now be examined.

The new economy is characterized by basic advances in ICTs, transportation technologies, biotechnologies and new-materials sciences. Such technological gains have boosted significantly the efficiency, effectiveness and flexibility productivity of business enterprises, among other human endeavours. The same uplift can also be gained by SMEs both directly and indirectly, as discussed in Chapter Four.[46]

In the above context, the issue is not whether to assist SMEs to invest in ICT-based facilities and services. Surely many SMEs, especially those on the top layers in priority industries and sectors in the region, will have "to go with the flow" of electronic interactivity, or be crushed by it. Rather, the issue is how best to encourage SMEs to make the most cost-effective use of the new technologies in production, marketing and networking.[47]

B. Current efforts and issues

A word of caution is necessary, however. Firstly, digital connectivity among SMEs and the amount of e-commerce have shown a tremendous expansion from the last decade. Such an upswing, however, has been highly concentrated in North America and Western Europe, as pointed out earlier.

[45] The quality, relevance and accessibility of domestic institutions for education, training and extension services feature prominently in the above context. In addition, what are the optimum combinations of public and private sector involvement in the provision of ICT infrastructure and services for all players and actors, including SMEs? Moreover, given the severe resource constraints in most developing countries, how should ICT infrastructures and facilities be distributed between domestic regions, or between the rural and urban areas etc?

[46] One is mediated through access to the global store of knowledge and market information. Secondly, new and innovative modes in industrial organization and enterprise management confer significant gains in efficiency and flexibility, in addition to reducing transaction costs and building up trust. This applies especially to collaborative linkages and partnering in production, or in research and commercialization both within and across borders. There is, lastly, the great potential of e-commerce itself.

[47] PricewaterhouseCoopers (1999) contains a useful survey of the main issues and options relating to e-commerce and SMEs in the APEC region. Debroy (2001: 37-43) provides a sober view on "www" in the Indian context – namely where will the ICT diffusion happen (urban and/or rural areas?) and who will facilitate it (private initiatives or government?). A detailed consideration of e-commerce in the context of low-income countries and economies in transition, specifically China, can be found in UNCTAD (2001: 189-250).

Closer to home, there is also a positive correlation between the reliance on ICTs and e-commerce on the one hand, and the state of socio-economic development, (such as the level of per capita income) on the other hand. Singapore and Malaysia, for example, are on one side of the spectrum as regards the basic prerequisites of ICT penetration. The other side of the spectrum are occupied by the four newer member countries of ASEAN. Other member countries are found somewhere in-between (see Table V-1 below).

Table V-1

Some Indicators of ICT Penetration in East and South-East Asia, 2001

	Computer density	Telephone main line density	Cellular mobile subscribers	Internet users density (per 10,000 persons)	Total Number of ISP	Population (millions)
	(per 100 persons)					
China		13.8	11.17	260.0	936	1,296.1
Japan		59.7	58.76	4,547.1	4000	127.3
Republic of Korea	25.1	47.6	60.84	5,106.8	99	47.7
Brunei Darussalam	7.5	24.52 [a/]	28.94	1,044.8	2	0.3
Cambodia	0.2	0.3	1.66	7.4	2	13.4
Indonesia	1.1	3.7	2.47	186.2	60	214.8
Lao PDR	0.3	0.9	0.52	17.7	2	5.6
Malaysia	12.6	19.9	29.95	2,395.0	6	23.8
Myanmar	0.1	0.6	0.03	2.1	1	48.4
Philippines	2.2	4.0	13.70	259.3	51	77.1
Singapore	50.8	47.1	72.41	6,051.5	42	4.1
Thailand	2.7	9.4	11.87	556.1	18	63.6
Viet Nam	1.0	3.8	1.54	49.3	4	81.1

Source: ITU website <http://www.itu.int/>, 4 December 2002.
a/ Data for the year 2000

Secondly, some one-half and one-third respectively of the medium and small-sized companies in Europe maintain an e-mail contact address or www presence (see Chapter Four). There is, however, no similar or comparable information available in the case of SMEs in the region.

A survey by PricewaterhouseCoopers indicates roughly that some three-quarters of the SME respondents among low- and middle-income economies of APEC have low levels of ICT-based e-commerce capabilities (1999: 7). However, this percentage reflects those enterprises on the top layers in their own industries and sectors only. The result cannot be extrapolated across the SME sector because the survey was not carried out on the basis of a random sample.

Thirdly, two other observations can be drawn from the cursory evidence available. One, the very large bulk of SMEs in most ASEAN countries has no on-line capabilities for all practical purposes. A very small proportion may have very basic capabilities and an even tinier percentage, a website presence and some ICT facilities for inter-firm networking purposes and other cyber transactions. Two, an extensive agenda has to be accomplished before large segments of the SME sector in developing countries of East and South-East Asia can be transformed into the so-called “virtual” enterprises and cyber entrepreneurs. This is

because of the wide ranging and, in several instances, deep-seated constraints on ICT penetration and e-commerce in many parts of Asia.

Clearly, the development of ICTs and e-commerce or, for that matter, of financial and capital markets is a long-term process with multi-dimensional implications on resources, both physical and human. As is evident form the above review, a myriad of problems and constraints remain although most of them are beyond the scope of this policy blueprint.

The five suggestions made in Chapter Six are thus of a transitional or bridging nature. They address a number of key, short-term issues whose resolution will serve two purposes. One is to facilitate of ICT penetration and e-trade reliance within the SME sector. The other is to promote higher levels of e-trade among regional SMEs as well as between them and those outside the region (as mediated through NIP and cross-border supply chains).

VI. Finance

The chronic lack of an adequate and affordable access to long-term credit, working capital and bridge financing is another well-known constraint facing the large bulk of SMEs in the developing countries. It is an intractable issue, firstly, because of several major imperfections in the financial markets. Secondly, some critical primary and secondary markets do not exist altogether in several countries, those for SME equity and bond financing especially.

Meanwhile, the financial intermediation process of many existing financial institutions leaves much to be desired – especially in terms of operational efficiency, the range of products and services on offer, and geographical coverage and outreach. On the other hand, many SMEs are unable to meet institutional requirements for standard accounting and other financial and business information. The availability of loan collaterals and business plans of an acceptable quality is another difficult constraint to alleviate and resolve.

A. Context and constraints

The formal banking sector continues to be the dominant source of capital and credit for domestic business among developing countries, those in ASEAN included (more later). In this respect, concerted efforts have been made by government in developing countries, including ASEAN, to allocate formal-sector resources and funds in support of SME sector development and integration.

The main channels are through commercial banks which have been encouraged or even directed to lend to SMEs by means of loan quotas, interest subsidies, tax breaks, and guarantees against default and so on. In addition, there are specialized financial institutions which focus directly on fostering small businesses and industries – such as agricultural, industrial and other sectoral development banks.

Indirectly, the qualified or targeted SME segments are also provided with financial support in cash and/or in kind under various programmes and projects. These tend to be more focused and highly specific in their operations – such as in start-up and linkage promotion (especially of an employment-intensive or high-tech nature), technological

upgrading, export market penetration, worker training and skill-base expansion, participation in trade fair and product exhibitions etc.[48]

With few exceptions, financial support measures and the massive subsidies involved in SME financing have not been as successful as intended. This applies in terms of the extent of outreach, cost efficiency and hence sustainability. Indeed, limited outreach at disparate cost (to government and the target beneficiaries themselves) is the perennial weakness of SME financing from the formal financial sector in a large number of developing countries, including several from ASEAN.[49]

As a result, most SMEs cannot secure bank loans, let alone on satisfactory terms. The cursory information indicates that altogether, SMEs may share less than one-quarter of the institutional credit and financial resources available to all business enterprises domestically. This relative stake tends to be lower than the SME sector's contribution to aggregate production. It is, however, significantly much less than SMEs' share in domestic employment generation (see Box V-8 below).

[48] For the more recent and specific details on various programmes in favor of SMEs, see Hew for Singapore (2002: 9-14), SMIDEC for Malaysia (2002: 12-13), Viloria for Philippines (2001: 135-159), Urata for Indonesia (2000: 21-26), and Mizutani for Thailand (1999).

[49] Sahami-Malmberg (2000: 117-119). Viloria (2001: 135-159) and Urata (2000: 21-45) contain a detailed examination of the problems and bottlenecks in SME sector financing in Philippines and Indonesia respectively. Such difficulties are, by and large, also typical in other developing countries in the region although the similarities may not be identical in terms of the extent of the problems and constraints, and their order of magnitude.

Box V-8. Barriers and Constraints in Bank Financing of SMEs

Survey data on SMEs and commercial bank financing are very limited and far from comparable. They also cover mostly SMEs at the top layers in their own sectors or industries. Moreover, even with such limitations, the data are available only for a few ASEAN countries. Nevertheless, several observations can be made from the survey results and other information.

Firstly, to meet long-term needs, around three-quarters up to as high as 90 per cent of SME entrepreneurs rely largely on their own savings, on short-term (unsecured) borrowings from relatives and friends, and on funds from the informal or grey markets. Such funds are revolving for credible customers although the interest rates charged on them are prohibitively high.

Secondly, between 3 and 18 per cent of SMEs in the top layers have some access to formal sector finance. In particular, almost two-thirds of the surveyed SMEs in the garment industry have accounts at commercial banks in Indonesia. Yet, less than one-fifth has ever applied for and actually obtained bank loans. As regards SMEs in the wood furniture industry, the corresponding figures are 47 per cent and less than one-tenth (van Diermen, 1997).

Thirdly, even when such credit is available, SMEs generally have to pay a higher rate of interest and comply to more restrictive terms and conditions, compared to those accorded to their large-scale counterparts. The real issue is access to finance, and not the interest charged on credit as such. Financial sector interest rates, even if adjusted for higher lending costs and risks, are still far below those from the curb or gray markets.

Fourthly, on the financial supply side, many financial institutions (from the formal sector) have been unable to operate profitably with SMEs as their sole or major debt clientele. This is because of higher lending costs, and greater difficulties in loan monitoring and payment collection.

In particular, there is an inverse relationship between loan sizes and transactions expenses in lending. In Indonesia, for example, the later may be as much as 26 per cent of the credit amounts of US$ 250 or less. Lending costs fall to less than 3 per cent for loan sizes larger than US$ 2,500 (Urata, 2000: 30).

Fifthly, the observed reluctance of commercial banks in dealing with SMEs is also due to the lack of quality collaterals, and of good and standardized financial data on the part of SMEs. A compounding factor is the commercial banks' own inadequate expertise to evaluate the potential of a SME project and the SME capacity for loan repayment. Moreover, commercial banks do not normally engage in long-term lending.

Sixthly, on the funding demand side, SMEs tend to have high rates of bankruptcies. Besides, they also depend heavily on the founding, individual entrepreneurs. Meanwhile, there are the long lead times (from loan negotiations, processing and approval), and complicated paperwork and documentation from formal-sector loan providers. These can cause missed opportunities and, more generally, reduce the motivation of SMEs to approach banks for loans.

B. Current efforts and issues

1. Equity and bond financing

Diversification of enterprise financing away from banks toward capital markets is a step in the right direction. This is because, historically, non-bank financial intermediaries will assume an increasingly important role in domestic and external resource mobilization along the path of economic and social advancement and transformation over time.

In the (pre-crisis) mid-1990s, for example, bank credit accounted for as much as three quarters of domestic investment finance, compared to around one-third in the United States or Australia. In particular, corporate debt securities were equivalent to 46 per cent of the combined GDP of the G-10 group of developed countries (World Bank and IMF, 2001: 363). However, the stock of outstanding bank loans in East and South-East Asia was about 100 per cent of the region's GDP, compared to about two-fifths in the major emerging economies outside Asia.

Significantly, the financial and economic crisis of 1997-1998 carries with it two important implications. Firstly, over-dependence on bank finance tends to increase financial systemic risks, including through the contagion (or cascading) effects. Secondly, corporate governance problems (which pre-existed or are prevailing) will accumulate without outsider control functions, such as those of capital markets.

Thus, a sine qua non (prerequisite) of both domestic and international equity and bond markets is the full disclosure of relevant information. Such disclosure pertains to both financial accounts and corporate governance standards; it also applies in both form (standardized format and timely presentation) and substance (transparency and usefulness). Without such information, the potential investors and rating agencies (both domestic and external) will not be able to assess the quality of the pertinent (company equity) stocks or (non-bank) debt instrument papers (securities or bonds).

Several countries in Asia have considered a dedicated capital and equity market in favour of SMEs and other young companies with an outward orientation and/or high potential for growth.[50] Generally, however, the response from SMEs has been less than enthusiastic.

As in the case of ICTs (discussed in the previous section), many enterprises are not fully aware of the comparative benefits of capital markets. It also does not help that many equity markets are subject to a significant amount of speculation. At the same time, there are relatively tedious registration procedures for regulatory issues of papers as well as the small number of underwriters for such issues.

[50] For example, concerted efforts have been made since July 1998 to set up the SME capital market, which was an initiative of the Philippine Stock Exchange. The listing requirements include (1) authorized capital of US$ 0.4-2 million with paid-up capital of at least one-quarter of the authorized amount; (2) two-year positive net operating income; (3) minimum offering size of one-fifth of the authorized capital; (4) lock-up period of three years; (5) existing owners to retain 51 per cent of equity holding; (6) the number of shareholders should be at least 50 persons. SMEs must undergo a nomination and listing process before they can join the SME capital market (Viloria, 2001: 150-151).

In addition, SMEs are also apprehensive of "going public" for a variety of other reasons – including notably taxes on initial offerings and on share transactions, and the relatively tight listing requirements and information disclosure. In this context, the disclosure requirements as regards accounting, financial and corporate governance information remain one of the most challenging hurdles for the large majority of SMEs.

2. Supplementary financing arrangements

A number of new and innovative credit schemes and financial instruments have been introduced in order to circumvent some of the difficulties and constraints in bank financing noted above. Again, experience has shown that there are no short-cuts or magic bullets to resolving certain highly intractable issues in SME financing.

Credit guarantee schemes have been set up in many developing countries to encourage banks to lend to SMEs. Premium levels of 1-4 per cent are charged on guarantees of up to 60-80 per cent of the loan amounts; however, premiums can be as high as 5-6 per cent in riskier cases. Most guarantee funds cover investments in production and technologies, and are generally not available for working capital purposes.

Numerous credit guarantee schemes have been in operation in East Asian countries, many for several decades (e.g., those in Malaysia, Philippines, Republic of Korea, Singapore and Thailand). By and large, their experiences are mixed (Levitsky, 2000: 126-130; and Sahami-Malmberg, 2000: 119-120).

It is pertinent to note that the Republic of Korea has one of the largest SME credit guarantee scheme among East Asian countries. The outstanding balance of guarantees provided for bank loans, bonds, commercial bills and leasing went up from US$ 13.4 billion in 1993 to US$ 17.2 billion in the pre-crisis year 1996, and to US$ 28.2 billion as of June 2000.[51]

With few exceptions, most guarantee funds are capitalized by donors and/or governments, and there are the related issues of sustainability (of guarantee fund allocations), bureaucratic interference and managerial professionalism. Documentation requirements may be less demanding but, in any case, the SME applicants' eligibility must again be re-appraised (in addition to a prior assessment from the commercial banks) before a credit guarantee is given (see Box V-9 below).

Venture capital is comparatively a more recent phenomenon in developing countries. It can provide SMEs with equity funding and the associated technologies, managerial assistance, and marketing access or expertise. Capital resources come from private and/or public sources. There are venture capital schemes in many ASEAN countries. As a whole,

[51] Guarantees are underwritten by the Korea Credit Guarantee Fund, established in 1976, and the Korea Technology Credit Guarantee Fund, set up in 1989. The government substantially increased its contribution, allocating US$ 2 billion to enable these two funds to meet their increased obligations and claims in the wake of the economic and financial crisis. The allocation consisted of disbursed loans from the Asian Development Bank and the World Bank. See Kang (2002: 188-196) for further details on SME financing, and related issues, in the Republic of Korea.

however, this financing modality tends to have a poor track record in many developing countries.[52]

Generally, SME entrepreneurs are reluctant to approach venture capitalists for fear (rightly or wrongly) of losing control and ownership of their enterprises, or of their original project ideas. At the same time, venture capital fund managers do not pursue SMEs aggressively because of the lack of project information, transparent operational records and credit rating (Timmons, 1990: 425).

Institutionally, the absence of equity and secondary capital markets renders the exiting (or withdrawal) process for venture funds difficult. In addition, most SMEs are not listed in equity markets and this accounts, in part, for the preference of many venture funds for the realization of quick and large profits in the immediate to short terms, instead of equity appreciation. Other problems also exist -- especially in terms of managerial experience, efficiency and professionalism (see Box V-9 below).

[52] Returns of minus 1 per cent to 5 per cent on venture funds are reported by the International Finance Corporation of the World Bank in the 1980s. A large number of venture capital funding schemes sponsored by the United States Agency for International Development have become insolvent or were liquidated (Sahami-Malmberg, 2000: 121).

Box V-9: Brief Assessment of Financial Means for Supplementary SME Financing

1. Credit Guarantee Schemes

Advantages

- *Risk sharing with banks and quick disbursement of loans*
- *Longer-term loans for sound projects*
- *Less stringent collateral requirements*
- *Additional loan assessment and appraisal done by guarantee organization*
- *"Learning curve" process for banks (to recognize reliable borrowers on the basis of past record of payments)*
- *Lenders not provided with cheap subsidized credit*
- *Possibilities of high leverage of guarantee fund to multiply the funds available for loan guarantees*

Disadvantages

- *Banks are reluctant to assume risks with low guarantee thresholds (e.g., less than 80 per cent of loan amount), and to lose control on their loans*
- *Possibilities of "moral hazard" problems (weaken commitment of borrowers to repay loans and lenders to collect repayments)*
- *Cumulative transactions costs (bank and guarantee fees) can be prohibitively high*
- *Time consuming and often inefficient settlement of bank claims on guaranteed loans*
- *Dependence on soft funds from donors and government*
- *Difficult to operate in a weak financial system*

2. Venture Capital Funds

Advantages

- *Providing flexible, longer-term equity capital*
- *Customized injections of managerial expertise and advice, and acquisitions of appropriate technologies*
- *Possibilities of ancillary or additional assistance in working capital, leasing arrangements, export marketing and financing*

Disadvantages

- *Difficulties in exiting or extracting equity funds in countries without a stock market or with an underdeveloped capital market.*
- *Withdrawal of invested (venture) capital may create serious difficulties in the operations of the pertinent enterprises*
- *Hard to find experienced and effective managers for venture capital funds in developing countries.*
- *Difficult to attract investments in (venture) funds with a primary focus on risky businesses without detailed credit and other profiles in developing countries.*

Equipment leasing allows SMEs to use a high-value asset (and the built-in, innovative technologies) in exchange for periodic payments to the equipment owners (or lessors). Again, leasing arrangements are available in most ASEAN countries. Their coverage ranges from office machinery to aircraft. Generally, equipment leasing tends to proliferate and thrive after or during a certain or specific stage of economic development (Levitsky, 2000: 131-132).

Typically, a security deposit of 10 per cent of the equipment value is required and the lease terminates after 5 years. Leasing is thus equivalent to medium-term financing. It facilitates SMEs' access to highly expensive machinery (looms, energy and office equipment and systems, transportation and assembly machinery etc.) with some transfer of technologies as well (see Box V-10 below). Delinquencies tend to be low, with some lessors reporting default rates of 2-7 per cent.

Inventory financing (also known as factoring) is a short-term arrangement. It enables SMEs to cover working capital needs (as absorbed in the accumulated inventory stocks). It is especially relevant in cyclical or seasonal businesses, as a means to acquire inputs (or to build up stocks) for continuous production (or delivery) throughout the year (see Box V-10 below). As collateral, inventories can generally bring in funds equal to one-half of their replacement value.

Box V-10. Brief Assessment of Non-financial Means for Supplementary SME Financing

1. Equipment Leasing

Advantages

- *Less stringent collateral and security requirements (the adequacy of cash flows to service lease payments being the primary consideration).*
- *Speedy arrangements and ready access to modern machinery and equipment*
- *Equipment well maintained and repaired, thus lowering down times*
- *Leasing payments being an operating costs rather than a financing charge.*
- *Good accounts-keeping for accurate forecasting of cash flows*
- *Availability of specialized companies or services for leasing, lease procurement, and leased equipment insurance*
- *Leased equipment cannot be used as collateral*
- *Lease payments may be high (as equipment may not worth much after the lease period due to technological obsolescence, over-use etc.)*

Disadvantages

- *Dependence on tax-based incentives*

2. Inventory Financing

Advantages

- *Tied-up working capital to be used as collateral*
- *Easier access to financing than through bank loans*
- *Possibilities of year-round production, and of purchasing inputs and disposal of outputs at advantageous prices or times*

Disadvantages

- *Detailed accounting of production and inventory turnovers*
- *Availability of acceptable warehousing security receipts and inventory quality standards*
- *Specialized companies to be established for the purposes of warehousing, and inventory control financing and insurance.*

Generally, financial sector development and, for that matter, the establishment of ICT infrastructure is a long-term process with multi-dimensional implications on resources, both physical and human. The very high saving rates (by global standards) in most economies of East and South-East Asia are a highly positive push factor in that context. A myriad of problems and constraints remain although most of them are beyond the scope of this policy blueprint.[53]

The four specific suggestions made in Chapter Six deal largely with the sine qua non of formal sector financing in the context of SMEs. They relate to the needs for adequate financial disclosure and communications on the financing demand side. On the institutional financial supply side, it is also necessary to enhance the roles and contributions of credit rating facilities as well as credit information and referral systems, especially those dedicated to SMEs.

VII. Conducive policy environment

Public-sector policies, institutions and regulations exert a profound impact directly on the behaviors of firms, including SMEs. Their indirect effects are transmitted and mediated through the input and output markets that business firms depend on, and through the expectations and responses of consumers and investors within and across borders as well.

A. Context and constraints

It is thus necessary and, indeed, well appreciated that the objectives, approach and design of economic and social policies, regulations and institutions must meet a number of requirements. One, they must be coherent and consistent across sectors and industries, and over time too. Two, they must also be transparent and predictable in their operation; moreover, an adequate measure of accountability is necessary in the implementation process.

In practice, however, it is virtually impossible to achieve all these requirements for consistency, coherence and transparency in most developing countries. This is also true in the current conditions and circumstances within most parts of ASEAN (see Box V-11 below).

[53] For further details on these problems and constraints, see ESCAP and ADB (2002), pp. 1-24) and World Bank and IMF (2001, pp. 360-385) plus the extensive references cited in the latter publication.

Box V-11: Inherent Constraints and Unintended Biases

Firstly, policies and regulations often have an unintended, adverse impact on SMEs because of various inconsistencies and trade-offs in their objectives, and hence in their outcomes. Taxes on exports, for example, are often imposed to raise government revenue or to conserve the exportable products for home consumption. By default, they also discourage SMEs and other enterprises engaging in such tradable production.

Likewise, the exchange rate may have to be devalued, and the interest rates raised for crisis prevention or stabilization purposes. But such measures also increase the financial costs of enterprises, both large and SMEs, in their operations and investment. Moreover, they penalize those firms which rely more on imports. Indirectly, they reduce domestic consumption, including consumer spending on SME-related goods and services

Such unintended side effects are a matter of significant concern. Compared to that shouldered by the large firms, these adverse effects are often heavier on SMEs on account of their smaller scale of operations as well as their more limited resources or access to resources. In addition, SMEs have more and greater needs in capacity building and extension services in the effective management of responsive changes.

Secondly, the legal, regulation, planning and tax frameworks can also be very complex. The formal registration of SMEs, particularly of those which are the target beneficiaries of government support policies, will have to be undertaken. However, the level of bureaucratic red tape encountered in the process can be daunting in many instances.

Depending on the types of business involved, the SMEs concerned may have to navigate through a bewildering menu of rules and regulations for registration purposes. Licenses, permits and clearances from a variety of agencies and bodies may take months to be obtained. The configurations of permits and clearances are also different in different countries. There is thus a solid justification for a serious trimming of the rules book to make it easier for the SME entrepreneurs to get started (Chow, Tan and Choong, 2002: A18)

More generally, opaque discretion, over-bearing regulations and expensive delays will raise transaction costs, imposing again a disproportionately heavy burden in time and expenses on SMEs for compliance purposes. All these can become a major impediment to the successful start-up, upgrading, expansion and diversification of many small businesses. At worse, they can encourage non-compliance activities, corruption practices, and the proliferation of the gray markets or underground enterprises and transactions.

Thirdly, the well-known "perverse incentive syndrome" facing most SMEs poses another compounding factor. This scale-based bias originates from the minimum requirements in production volume, local contents, capital investment and/or export levels as a pre-condition for government incentives and assistance.

There are valid economic, financial and technological reasons for granting benefits and privileges in exchange for certain minimum or baseline conditions or stipulations. These reasons include, for example, prospective economies of scale and scope, greater employment volume and market penetration, easier transfer and dissemination of new technologies, better

intellectual property and environmental protection etc.

However, ways and means have to be devised to minimize such a size-based policy bias. Compensatory measures may include the provision of inducements and assistance in the formation, widening and deepening of both backwards and forwards linkages with smaller scale suppliers and providers of goods and services.

An enabling policy and institutional environment matters even more in the context of macroeconomic reforms and adjustments. By default or accident, such changes have often been made without adequate preparations and judicious sequencing. They are also not underpinned by the widespread dissemination of information, guidebooks and toolkits to assist domestic enterprises in reaping the emerging opportunities and meeting the associated challenges.

Among the pertinent examples are a variety of commitments made under global and regional trade agreements; the extensive liberalization and deregulation of domestic (factor and product) markets, including the FDI regimes; expenditure-compressing measures undertaken as part and parcel of the crisis stabilization process and so on. Some of these measures have generated highly adverse effects on the SME sector.

In fact, large segments of the SME sector have ceased operations, or have lost much ground in terms of competitiveness in recent years. There are now, for example, several detailed studies on the damaging impact of the financial and economic crisis on SMEs and their responses to the crisis from July 1997 (Urata, 2002; Regnier, 2000; Tambunan, 2000; and van Diermen, 1999)

B. Current efforts and issues

Undeniably, it is very difficult to eliminate conflicts in policy objectives and to remove policy trade-offs across sectors and industries. Nevertheless, efforts must still be made to crowd in, and not to crowd out, SMEs in the design and implementation of policies and institutions. The agenda for consideration is extensive, given the current conditions and circumstances in most developing countries, including many within ASEAN.

Firstly, it is not that political commitment in support of SME sector development and integration is lacking in the above context. Rather, such commitment at the national and regional levels may need better articulation, more concrete manifestations, and hence greater and more consistent visibility. Some of the possible ways and means to resolve some of these issues are discussed in Chapter Six.

Secondly, as regards the “rules of the game”, it is clear that SME support policies, programmes and projects have to satisfy some challenging benchmarks. They have be more effective in terms of outreach, more focused in efficiency-oriented targeting, more efficient in relation to cost and financial sustainability, and more flexible for better and more timely responses to changing needs and demands.

On the other hand, the costs (in cash and kind) of SME transactions and participation in public-sector policies, programmes and projects must not be burdensome. This can be attained gradually with greater consistency, coherence and clarity in policy design. In addition, a more judicious sequencing of policy changes, complemented by an extensive dissemination of high-quality information, would speed up the adjustment process (whether positive or defensive in nature) for SMEs.

Thirdly, greater coordination and synergies are called for among public-sector institutions and offices dealing with SMEs, whether directly or otherwise. In some countries, there is a multiplicity of official institutions with responsibilities for SMEs. Bureaucratic mindsets and rigidities are issues to be satisfactorily resolved. Meanwhile, the protection of vested interests, inter-agency rivalries, conflicts of interests, and disruptive delays and miscommunications have been an unavoidable by-product.[54]

A related issue is the need for better management of policies, programmes and projects. This applies not only at the design and targeting stages. Performance management is especially pertinent in the tracking and evaluation of the delivery process and its impact on the intended target beneficiaries (see Box V-12 below).

[54] It is possible that some SME promotion programmes and projects are approved by certain official bodies but are altogether over-ruled by, or subject to excessive delays in, other institutions on account of actual or alleged constraints on resources or technical factors within the inter-agency appraisal process.

Box V-12. Performance Management

What gets measured gets managed. But good performance evaluation is not possible without good performance information and data. However, a systematic, objective and timely assessment of the impact and results of policies, programmes and projects is not an end in itself. It is but a tool to help improve performance management which itself should be the focus of attention.

There are two related issues. One is the collection of performance information and data -- including indicators of policy, programme and project impact. The main elements of this process, which is highly complex in itself, can be seen in the indicative roadmap on performance measurement contained in Chapter Seven.

The second issue relates to an institutional capacity to process and analyze, store and update, and utilize and publicize the information and data so collected. This particular aspect of performance management often is not accorded due recognition and provided with the needed resources.

Fourthly and likewise, there should be a development partnership among the main stakeholders with a mandate or interest in SME sector development and integration. The players and actors involved can be domestic such as government and non-government bodies. They can equally come from both inside and outside the ASEAN region, thus endowing the interaction and dialogue process with a regional and international character.

Such a partnership will, among other things, facilitate more regular interactions and consultations among all concerned. This will help to minimize the unintended policy constraints and other inconsistencies as regards SMEs, provided that the sector is well represented in the process.

A synergic partnership will also lead to a more rational division of labour between the public and private sectors in the provision and diversification of BDS and extension activities in support of SMEs. This applies especially to the need for more direct response to demands from, and to ensuring greater cost sharing by, the target beneficiaries over time. The subsidiarity principle is pertinent in these regards, as will be discussed in Chapter Six where seven functional proposals will be made.

Chapter Six

RECOMMEMDED POLICY APPROACHES, MEASURES AND OPTIONS

Contents

The current conditions, new paradigmatic context, and constraints regarding SME sector development and integration were examined at length in Chapter Three through Five respectively in the proposed policy blueprint. Against that backdrop, the following discussion maps out in detail a series of proposals in support of the ASDD 2002-2012.

I. Overview of policy proposals

Table VI-1 below contains a bird's-eye view of the policy approaches, measures and options recommended in the blueprint. These recommendations are given with special reference to the corresponding activities suggested for implementation under the RAP for the ASDD 2002-2012.

A. Complementarities between the Action Plan and Policy Blueprint

The supportive and mutually reinforcing nature of these two sets of proposals is evident from the comparative presentation made in Table VI-1. As regards elements of regionality, it can be stated here that collaborative efforts are applicable to virtually all the recommended approaches, measures and options in the policy blueprint. These efforts, which indicated by the first two items for each suggested activity, can be mediated within ASEAN, as well as with ASEAN dialogue partners and organizations.

Co-operative interactions can take place at two levels. One relates to good and superior practices which can be distilled from regular dissemination of high-quality information, including that on success stories, and from periodic exchanges of views and policy experiences at both the intra- and extra-regional levels.

Two concerns the provision of human expertise and financial resources to initiate and/or sustain the momentum of wide-ranging activities carried out in fostering SME sector development and integration. This applies especially to co-operation measures between ASEAN-6 and ASEAN-4 as well as to collaboration between ASEAN and dialogue partners and organizations, plus other stakeholders (including civil society entities).

Table VI-1

Complementarities between the Regional Action Plan and the Proposed Policy Blueprint for the ASDD 2002-2012

Suggested activities under RAP	Suggested activities in the policy blueprint
1. On-line business matching	1.1 Dissemination of success stories, and good and superior practices -- by or through inter-linked, on-line networks of provincial or industry-based clearing houses or trading points for SME businesses, or the one-stop SME support office. 1.2 Exchanges of views and policy experiences within ASEAN, and with ASEAN dialogue partners and organizations with a view for follow-up assistance and collaboration. 1.3 Establishing inter-linked, on-line networks of provincial or industry-based clearing houses or trading points for SME businesses. 1.4 E-commerce facilitation and promotion by one-stop SME support-office.
2. Setting up sectoral and subsectoral databases of SMEs	2.1 Dissemination of success stories etc. (as in 1.1 above). 2.2 Exchanges of views and policy experiences etc. (as in 1.2 above).

	2.3 Survey of ICT and e-trade penetration within the SME sector 2.4 Surveying and benchmarking SME capabilities and competitiveness 2.5 Monitoring SME subcontracting readiness and compliance to subcontracting compact 2.6 SME registration by one-stop SME support office.
3. E-commerce accreditation of SMEs	3.1 Dissemination of success stories etc. (as in 1.1 above). 3.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 3.3 Survey of ICT and e-trade penetration within the SME sector 3.4 Monitoring SME subcontracting readiness and compliance to subcontracting compact (or code of conduct). 3.5 SME registration and e-trade accreditation by one-stop SME support office
4. Feasibility of promoting industry clusters	4.1 Dissemination of success stories etc. (as in 1.1 above). 4.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 4.3 Surveying and benchmarking SME capabilities and competitiveness 4.4 Monitoring SME subcontracting readiness and compliance to subcontracting compact (or code of conduct) 4.5 Identified areas for further research on enterprise clustering.
5. Regional trading house	5.1 Dissemination of success stories etc. (as in 1.1 above). 5.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 5.3 Inter-linked, on-line networks of provincial or industry-based clearing houses or trading points for SME businesses. 5.4 Regional e-trade facilitation and promotion by one-stop SME support office 5.5 Government procurement by e-commerce and e-documentation
6. Widening export market financing for SMEs	6.1 Dissemination of success stories etc. (as in 1.1 above). 6.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 6.3 Demand-side prerequisites: availability of standard financial data and information, and well-prepared business plans from SMEs. 6.4 Supply-side prerequisites: institutional capabilities for rating and scoring of credit worthiness/risks, and availability of credit information reference and referral systems
7. Cabotage removal to reduce transaction costs for SMEs in regional trade	7.1 Dissemination of success stories etc. (as in 1.1 above). 7.2 Exchanges of views and policy etc. (as in 1.2 above).

	7.3 Reducing policy biases against and constraints on SMEs to lower (unequal) costs and burdens on them 7.4 Ensuring policy consistency and coherence in support of SME development and integration 7.5 SME-advocacy and facilitation functions by one-stop SME support office
8. Feasibility of setting up a regional venture capital corporation	8.1 Dissemination of success stories etc. (as in 1.1 above). 8.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 8.3 Demand-side prerequisites (as in 6.3 above). 8.4 Supply-side prerequisites (as in 6.4 above). 8.5 Widening and deepening the investor base, including through external linkages (e.g., subcontracting and inter-firm partnering) within and outside ASEAN
9. Promoting equity participation in indirect forms of SME financing	9.1 Dissemination of success stories etc. (as in 1.1 above). 9.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 9.3 Ensuring the availability of demand side prerequisites (as in 6.3 above) 9.4 Ensuring the availability of supply side prerequisites (as in 6.4 above). 9.5 Widening and deepening the investor base (as in 8.5 above).
10. Facilitating SME access to finance in other member countries	10.1 Dissemination of success stories etc. (as in 1.1 above). 10.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 10.3 Ensuring the availability of demand-side prerequisites (as in 6.3 above). 10.4 Ensuring the availability of supply-side prerequisites (as in 6.4 above). 10.5 On-going surveying and benchmarking SME capabilities and competitiveness 10.6 Monitoring SME subcontracting readiness and compliance to subcontracting compact (or code of conduct). 10.7 Widening and deepening the investor base (as in 8.5 above).
11. Development of new and innovative financing programmes and packages (such as factoring, credit guarantees, accounts receivables etc.)	11.1 Dissemination of success stories etc. (as in 1.1 above). 11.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 11.3 Ensuring the availability of demand-side prerequisites (as in 6.3 above). 11.4 Ensuring the availability of supply-side prerequisites (as in 6.4 above). 11.5 Widening and deepening the investor base (as in 8.5 above)..

12. Establishing rating systems for SME financing	12.1 Dissemination of success stories etc. (as in 1.1 above). 12.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 12.3 Developing rating and scoring systems for credit worthiness/risks, including those of SMEs 12.4 Setting up credit information reference and referral systems, including those for SMEs
13. Capital market development for SMEs (trading in shares/stocks, and bonds/securities)	13.1 Dissemination of success stories etc. (as in 1.1 above). 13.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 13.3 Ensuring the availability of demand-side prerequisites (as in 6.3 above). 13.4 Ensuring the availability of supply-side prerequisites (as in 6.4 above). 13.5 Widening and deepening the investor base (as in 8.5 above).
14. Enhancing best practices in building up and maintaining SME data bases	14.1 Dissemination of success stories etc. (as in 1.1 above). 14.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 14.3 Facilitation and outreach services, including database building and maintenance, from the one-stop SME support office
15. Developing regional data bases for sharing critical information with SMEs	15.1 Dissemination of success stories etc. (as in 1.1 above). 15.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 15.3 On-going surveying and benchmarking SME capabilities and competitiveness. 15.4 Monitoring SME subcontracting readiness and compliance to subcontracting compact subcontracting compact (or code of conduct). 15.5 Facilitation and outreach services, including database building and maintenance, from the one-stop SME support office
16. Facilitating the free flow of information technology to increase SME business opportunities	16.1 Dissemination of success stories etc. (as in 1.1 above). 16.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 16.3 Distribution of high-quality information on technology and intellectual properties from inter-linked, on-line networks of provincial or industry-based clearing houses or trading points for SME businesses. 16.4 Facilitation and outreach services, including distribution of high-quality information on technology and intellectual properties, from the one-stop SME support office.
17. Encouraging the development, transfer	17.1 Dissemination of success stories etc. (as in 1.1 above). 17.2 Exchanges of views and policy experiences etc. (as in 1.2

and exchange of technology among SMEs	above). 17.3 Self-reliant building up of organizational and managerial capabilities, and other skills in production and marketing. 17.4 Compliance with subcontracting compact or code of conduct 17.5 Monitoring and benchmarking of SME capabilities and competitiveness 17.6 Dissemination of good or superior practices, and of success stories in technology development, transfer and exchange from inter-linked, on-line networks of provincial or industry-based clearing houses or trading points for SME businesses. 17.7 Facilitation and outreach services from the one-stop SME support office, including through the distribution of good or superior practices, and of success stories in technology development, transfer and exchange.
18. Standardizing "SME experts" for regional certification	18.1 Dissemination of success stories etc. (as in 1.1 above). 18.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 18.3 Externally certified trainers in entrepreneurship development for training activities within ASEAN. 18.4 Certified toolkit (and guidebook and user manual) developers for carrying out related extension activities within ASEAN to promote self-reliant capacity building by SMEs
19. Standardizing skilled labour for regional certification	19.1 Dissemination of success stories etc. (as in 1.1 above). 19.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 19.3 Externally certified trainers in entrepreneurship development for training activities within ASEAN. 19.4 Internship, workers' exchange, and skill training and enhancement schemes within ASEAN.
20. Developing a supply pool of entrepreneurs (through training, making cross-cultural studies, entrepreneur exchange and internship schemes, and women entrepreneur promotion)	20.1 Dissemination of success stories etc. (as in 1.1 above). 20.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 20.3 Sustained efforts in SME entrepreneurship development through training and linkage promotion. 20.4 Capacity building of SME entrepreneurs and managers in enterprise organization and management, including in accounting and business plan preparations, on a self-reliant and cost sharing basis, as appropriate. 20.5 Promotion of inter-firm networking and internship schemes, including through periodic monitoring of SME subcontracting readiness or compliance to subcontracting compact (or code of conduct). 20.6 Training, advocacy and facilitation by or through the one-stop SME support office.

21. Assessment of SME capabilities (including through factory diagnoses, and competitiveness benchmarking)	21.1 Dissemination of success stories etc. (as in 1.1 above). 21.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 21.3 On-going surveying and benchmarking SME capabilities and competitiveness 21.4 Monitoring SME subcontracting readiness and compliance to subcontracting compact (or code of conduct) 21.5 Self-reliant capacity building in enterprise organization and management 21.6 Training, advocacy and facilitation by or through the one-stop SME support office.
22. Promoting regional linkages among government, private sector and the academe	22.1 Dissemination of success stories etc. (as in 1.1 above). 22.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 22.3 Development partnership for SME development between the public and private sectors (including tertiary institutions and civil society organizations) through closer interactions and more frequent dialogues, and a rational division of labour in BDS and extension activities (the subsidiarity principle). 22.4 Joint trilateral programmes and projects in entrepreneurship development training. 22.5. Joint trilateral programmes and projects to develop and disseminate toolkit packages for self-reliant SME capacity building.
23. Employing overseas resources to promote market collaboration and penetration, technology transfers and quality enhancement	23.1 Dissemination of success stories etc. (as in 1.1 above). 23.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 23.3 Monitoring SME subcontracting readiness and compliance to subcontracting compact (or code of conduct) 23.4 Developing toolkits (and related guidebooks and user manuals) for self-reliant capacity building 23.5 Capacity building for quality certification, and for on-going improvements in quality, cost and delivery punctuality.
24. Training programmes to upgrade SME technological skills	24.1 Dissemination of success stories etc. (as in 1.1 above). 24.2 Exchanges of views and policy experiences etc. (as in 1.2 above). 24.3 Developing toolkits (and related guidebooks and user manuals) for self-reliant capacity building. 24.4 Technological capacity building for quality certification, and for on-going improvements in quality, cost and delivery punctuality

B. Focal areas in the proposed policy blueprint

In addition, there are many specific policy recommendations, including several pilot project proposals, which are not contained in the RAP. For ease of advance reference, Table VI-2 below provides a summary of the major suggestions, together with indications as regards regionality elements (RG) and implementation timeframes (TF).

Table VI-2

Some Focal Proposals in the Policy Blueprint

1. Major Pilot Project Proposals	***Characteristics***
1. Training course on SME entrepreneurship development – including the generation and overseas certification of local capabilities in such training, the preparation of business plans to the bankable stage, and the promotion of inter-firm linkages in the training process.	RG: regional to subregional to national levels. TF: Short term for pilot project; long-term for full-scale programme
2. Development of toolkit packages for self-reliant SME capacity building in two pilot areas – (1) quality control and certification, and (2) productivity enhancement in quality, cost, and delivery.	RG: same as in 1 above. TF: same as in 1 above
3. Measuring, assessment and benchmarking of SME capabilities and competitiveness in selected industries within ASEAN.	RG: same as in 1 above. TF: same as above
4. Compilation of the typical preconditions and prerequisites for subcontracting, and monitoring SME compliance to such a subcontracting compact or code of conduct.	RG: same as in 1 above. TF: same as in 1 above
2. Other Selected Areas for Policy Consideration	***Characteristics***
5. Simplification and standardization of basic terminologies for training courses in, and self-reliant preparation of, SME business plans and business projects – including local adaptation and translation of the compiled glossary, as appropriate	RG: regional or national level TF: short term
6. Policy-oriented research on specific determinants of the successful clustering of enterprises – with special reference to the lessons learnt, and the success stories gained, from enterprise clusters within and outside ASEAN.	RG: same as in 5 above TF: short term
7. Assessment of SME needs in ICTs and e-commerce, with special emphasis on software and hardware, internet connections and website design and maintenance issues.	RG: subregional or national level TF: short term

8. Compilation and dissemination of success stories, and good or superior practices in ICT-based transactions (including e-trade and e-documentation) experienced by SMEs within and outside ASEAN.	RG: same as in 1 above. TF: same as in 1 above
9. Policy-oriented research on a basic framework of modern and up-to-date policies and regulations on e-commerce.	RG: same as in 5 above. TF: same as in 5 above
10. Financing demand side: SME capacity building in (a) proper maintenance and reporting of accounting and financial information, and (b) business plan preparations to the bankable stage.	RG: same as in 1 above. TF: same as in 1 above
11. Financial supply side: institutional capacity building in (a) credit rating adaptable to better meet SME special needs, and (b) credit widening modalities (including guarantee schemes and venture capital).	RG: national to subregional to regional levels TF: medium to long term
12. Feasibility assessment of the regionalization of financing resources for SMEs – including through collaboration with ASEAN dialogue partners and organizations.	RG: regional or subregional level TF: short to medium term
13. Research study to identify and modify major inherent constraints on, and unintended biases against, SMEs in the policy, regulation and institutional framework.	RG: same as in 11 above TF: same as in 12 above same as in 11 above.
14. Simplification and streamlining of the registration procedures for SMEs.	RG: same as in 11 above TF: same as in 12 above
15. Policy-oriented study on ways and means to promote greater synergies and partnership between the public and private sector in support of SME development.	RG: same as in 11 above TF same as in 12 above
16. Policy-oriented study on ways and means to ensure greater and more effective representation of SMEs in public-private sector dialogues and interactions.	RG: same as in 11 above TF same as in 12 above

II. Entrepreneurship development

Entrepreneurs are not only born. They have to be identified, trained and nurtured with or through the provision of a variety of BDS and extension activities. In this regard, evidence from extensive cross-sectional research and behavioural studies indicates that entrepreneurship is not just personality trait, or a cultural characteristic.

A. Context and justification

Generally, the successful entrepreneurs exhibit some 21 sets of personal competencies which, in turn, can then be expressed and benchmarked through 67 indicators. The latent attributes and determinants of successful entrepreneurship are also widely distributed. More importantly, these characteristics can be identified through systematic screening, and then replicated through training across countries.[55]

Entrepreneurship can thus be fostered through training. In this connection, the proposed approach for entrepreneurship development in the policy blueprint is innovative in several aspects (see Box VI-1 below).

[55] Professor David McClelland, the Harvard social psychologist, was the principal force behind these significant findings on entrepreneurship development in from the late 1960s. Based largely on such findings and related research results in the following decades, a large number of training programmes on entrepreneurship development have since been devised and implemented across the globe. For a historical review and further discussions on this and related matters, see Tan (2002) and Timmons (1990), and the numerous references cited in these pieces of work.

Box VI-1. An Innovative Approach in Entrepreneurship Development

Firstly, there will be numerous applicants for capacity building in entrepreneurship, given the vast number of current and potential SME entrepreneurs in ASEAN (Chapter Three). It is thus essential to ensure and carry out vigourous, pre-training screening and objective selection of potential entrepreneurs, and of (existing) SME entrepreneurs with the best prospects for success.

Secondly, the programme must also help the selected and trained entrepreneurs to develop basic skills in the formulation of a bankable business plan. This has been one of the crucial stumbling blocks in the financing of many SMEs. Yet, such a plan has been, and will remain, a prerequisite in funding business start-up, expansion and diversification (see Chapter Five).

Thirdly, to maximize its utility, the training programme in entrepreneurship development must also provide opportunities for inter-firm linkages and collaboration. This process can be fostered with greater ease among the entrepreneurs who are undergoing, or have taken, the same training programme. As such, they are imbued with similar or common perceptions, motivations and knowledge as regards business development and linkages.

Fourthly, programme outreach and sustainability considerations require that local capabilities in entrepreneurship development training be created. This has to be built into the programme right at the beginning to ensure maximum cost effectiveness. Quality of local trainers is to be assured through training and certification overseas.

Fifthly, trained entrepreneurs will be monitored for a period of at least two years afterwards. This is to assess the impact of training on their business development as well as to provide additional BDS and extension activities, on a self-reliant basis if necessary. All trained entrepreneurs are also encouraged to form their own Alumni Association for linkage purposes, and for better articulation of and representation on matters of interest and concern to them.

The integrated approach suggested above should not be regarded as "picking winners". It is, instead, designed to conserve limited resources and maximize programme impact and outreach. This is to be achieved by ensuring the most cost-effective training available to the qualified recipients (whether they be current or potential entrepreneurs), and by creating opportunities for inter-firm networking and partnering.

Women entrepreneurs are an important segment of the SME sector, as indicated in Chapter Three. For this reason and for empowerment purposes, due emphasis is given to the promotion of women entrepreneurs' participation in the training and networking processes.

B. Proposals

It is both pressing and important that entrepreneurship development training be initiated and sustained, preferably at least through the ASDD 2002-2012. Thus, the programme to be implemented is of a long-term nature so as to help incubate a culture of entrepreneurship, innovation and networking at least within the SME sector. Equally important, it also embodies several elements of regionality and regional integration.

To begin with, a region-wide approach in developing entrepreneurship training programmes and activities will serve to maximize collective gains. This applies especially in negotiations with donors for (full or partial) funding and with service providers for costing and cost reduction. There are as well significant economies of scale and scope in the implementation process, particularly in setting up local infrastructure and facilities for long-term operations at the regional or subregional levels.

In addition, considerable assistance can be expected from ASEAN-6 to ASEAN-4 in training activities, thus furthering gainful business cross-fertilization and linkages. Externally certified training teams from the former will provide training services in entrepreneurship development to ASEAN-4 in the short term (1 to 3 years). This will take place along with the formation of intra- and extra-regional linkages involving SMEs from both groups of countries.

1. Training in entrepreneurship development

To ensure maximum cost-efficiency and outreach sustainability, local capabilities for training in entrepreneurship development have to be built-up for more widespread replication of training activities across sectors and countries. What are some of the major considerations and parameters involved? What outcomes are to be expected from such activities in entrepreneurship training and in training capacity building?

One, there are several ready-made training programmes on entrepreneurship development. Motivational programmes have generally performed well. The average training period is two weeks of full-time attendance, a duration judged to be optimal for the very intensive motivational interactions between trainers and trainees, and among the latter group too. The period is also sufficiently short to attract, and facilitate participation by the selected applicants.

Two, a training team of 2-3 persons is needed for each training cycle (of two weeks). Initially, the team may be non-ASEAN service providers and the language of communication will be in English. However, training materials can be translated and provided in the local language. This will continue for about 12-18 months, until local capabilities in entrepreneurship development training are adequate to take over the responsibilities.

Three, each training team can undertake around 12-16 training cycles per year, depending on the burden of follow-up monitoring as regards progress or problems encountered by the trainee entrepreneurs in carrying out their business plan and inter-firm linkage proposals. Each training class can accommodate a maximum of 25 trainees. Thus, some 300-400 entrepreneurs can receive training and the necessary follow up (direct or indirect) monitoring per training team each year (see Box VI-2 below).

Box VI-2: Building up Local Training Capabilities

Local trainers can be selected from the trained entrepreneurs who exhibit good skills in communication, motivation and inter-personal relations. Additional enrichment training and overseas certification will be required. The process can take 3-6 months although the actual training involved overseas is much shorter than that (4 to 6 weeks). The establishment and external certification of local trainers are best undertaken as a joint public-private sector initiative.

Most ASEAN-6 have a greater base in terms of both human resources and finance for the external certification process. At the initial stages, therefore, (externally certified) teams from these countries can assist in providing training in entrepreneurship development in ASEAN-4, until the adequate generation of local capabilities to take over the jobs among these newer ASEAN members. Programme implementation thus will proceed from the ASEAN regional to subregional and national levels.

A supply base of 10 (three-person) teams, totalling 30 local trainers (but several of them may have overseas certification), can provide training for 3000-4000 trainee entrepreneurs a year. This is a sizable number, if the process is sustained over a decade (30,000-40,000 trained and networked entrepreneurs).

Thus, assuming that each trained entrepreneur can provide employment for 5 additional workers during the first year of post-training operations and inter-firm linkages. Then the volume of extra employment generation is 15,000-20,000 persons a year (or 150,000-2000,000 persons a decade).

For economies such as Indonesia, Philippines, Thailand and Viet Nam, the supply base of training teams may have to be even larger to accommodate greater needs. The importance of joint public-private sector efforts and infrastructure is thus evident (1) in the creation of local training capabilities, (2) in the follow-up monitoring of the progress and difficulties encountered by the trained entrepreneurs; and (3) in the provision of additional or remedial BDS and extension activities, including those of a self-diagnosis and self-reliant nature.

2. Pilot project in entrepreneurship development

Table VI-3 below contains the various categories of output from a typical three-year project, involving GMS economies for illustrative purposes. The project is deliberately designed on the conservative side to ensure considerable over-delivery of planned outputs.

In particular, China is likely to be interested in training programmes in entrepreneurship development -- given the on-going divestiture of a large proportion of state-owned enterprises, and the progressive economic liberalization and integration into the regional and global economy. There is thus a great potential for ASEAN-China cooperation in the above regard as well as for ASEAN-China enterprise linkages (as a by-product of such training collaboration).

Pilot project activities are intended:

(1) to train between 3500 and 4000 GMS entrepreneurs;
(2) to graduate 10-12 GMS training teams (of 3 persons each) on entrepreneurship development;

(3) to arrange for the international certification of 6 local trainers;
(4) to assist in the preparation of some 800-950 business plans (as proposed by the trained entrepreneurs) to the bankable stage, including through the provision of follow-up BDS and extension activities; and
(5) to promote 240-320 business linkages and sub-contracting arrangements among the trained GMS entrepreneurs, as well as between them and other non-GMS business firm.

Table VI-3

Overview of Pilot Project Outputs

	Number of entrepreneurs trained	Number of 3-person local training teams	Number of (local) trainers certified overseas	Number of business plans assisted	Number of inter-firm linkages promoted
Cambodia	300-350	1		80-100	20-30
Lao PDR	150-200	1		40-50	15-20
Myanmar	400-450	1-2		120-150	35-50
Thailand	1 350-1 500	3	3	260-300	80-100
Viet Nam	900-1 000	3	3	175-200	50-70
Yunnan, China	400-500	1-2		125-150	40-50
Project total	**3 500-4 000**	**10-12**	**4-6**	**800-950**	**240-320**

Source: Lam and Wattanapruttipaisan (2001, p. 18)

The average cost is below US$ 900 for each of the 3500-4000 GMS entrepreneurs for a package which includes training as well as follow-up support services and extension activities for the four output categories noted earlier. More significantly, the average training and support cost will fall off steeply, by between 50 and 66 per cent, when (externally certified) local teams take over the responsibilities for training and back-up support fro entrepreneurship and SME development.

III. Self-reliant capacity building and strengthening

The proposed approach in dealing with the basic requirements in enterprise organization and management skills relates to the compilation, field-testing and distribution in a multi-media format of a wide range of system packages of toolkits. Such dissemination is to be complemented by the provision of related guidebooks and (users) manuals, and supplementary training and extension activities as necessary.

A. Context and justification

The system packages are expressly designed for self-reliance capacity building, problem diagnosis and trouble shooting, totally or largely by the targeted enterprises themselves. They are thus part and parcel of BDS and extension activities. The toolkit approach, as proposed, has significant comparative advantages on both the supply and demand sides (see Box VI-3 below).

Box VI-3. Cost-efficient and Effective Outreach

Regarding supply-side considerations, the system packages of toolkits can cover a wide range of areas and subjects directly pertinent to the basic capabilities needed by SMEs. Some of them are selectively listed in Box V-2 in Chapter Five above.

In addition, there are substantial economies of scale and scope in the development and finalization of a large number as well as range of toolkit packages, and their distribution in a multi-media format. The collective gains are even larger with a regional approach.

As such, the cost-efficiency in capacity building is far more significant than those possible or associated with many traditional programmes and projects in BDS and extension activities. Moreover, through multi-media distribution, the extent of targeted outreach is comparatively also far more extensive. This is an important consideration given the very large number of targeted SMEs in the top segments in priority industries and sectors.

Lastly, the toolkit development process can easily be a joint public-private sector effort. External collaboration is to be mobilized, especially as regards technical assistance and technology transfers in the ASEAN toolkit development process.

The process itself can also be suitably sequenced to respond more speedily, and in a more demand-driven manner, to changing priorities or needs associated with the evolving pace and patterns of supply and demand, both domestic and external facing the SME sector.

On the demand side, the availability of self-reliant toolkit packages will save much time and money for the SME beneficiaries themselves. This can be seen in several ways.

For example, the enterprises concerned can set up, adopt and be ready to practice quality management and/or productivity-enhancing systems at their own pace. Such “dry runs” can take place well before the registration for formal, third-party or ISO certification itself. The same systems can equally be tested well in advance of the scheduled or specified

improvements in quality, cost and delivery for contract production bidding, for business-matching or subcontracting purposes (more in the next section).

Generally, the self-reliant toolkit approach is particularly suitable for SMEs at the top layers in their respective sectors and industries. As discussed in Chapter Two, these firms are the primary target beneficiaries of the proposed policy blueprint. They are more able to engage in self-diagnosis and trouble shooting of problems and bottlenecks. They are also in a better position to share costs, in cash or in kind, inevitable in self-reliant capacity building. Moreover, their needs for BDS and extension activities tend to be more demand-driven in nature.

B. Proposals

Under an ideal scenario, toolkit packages should be available (from both the public and/or private sectors) at lease for all the areas of basic skills as listed in Box V-2 in Chapter Five above. However, such availability (let alone affordability and relevance) is not the case in most, if not all, parts of ASEAN, especially those currently in transition to a market-based economy.

1. Development of system packages of basic toolkit

As a whole, certain basic skills and expertise are generic or common to all enterprises. The depth and extent of relevance of some of them may vary with operating scale, or sectors and industries in which firms operate. Fine tuning will be needed for greater industry- as well as country-specificity in contents and illustrations. But this is should be part of the continuous revision and upgrading process to enhance the relevance and effectiveness of the completed toolkits in any case.

The range of basic or generic toolkit packages should cover the following:

- Strategic planning
- Market analysis
- Finance and accounting
- Repair and maintenance
- Manufacturing processes
- Materials and production management
- Product differentiation and development
- Packaging and distribution
- Quality control and assurance
- Information systems
- HRD and management
- Environmental management
- Logistics and infrastructure
- Networking and linkages
- Management of change

As in the case of training in entrepreneurship development, the toolkit development programme for SMEs is also of a long-term nature. New toolkit packages will need to be complied and tested to better reflect the growing complexity and changing nature of market demands and consumer preferences (discussed at length in Chapter Four). Equally

important, the toolkit development and application processes also embodies several elements of regionality and regional integration

A region-wide approach will maximize collective gains in several ways, as discussed in the last section. In addition, there will also be much assistance from ASEAN-6 to ASEAN-4 in the development of toolkit packages, especially those deemed of greater priority or urgency to SMEs in these newer member countries. Toolkit developers from ASEAN-6 can also provide support services for toolkit applications by SMEs in ASEAN-4 (see Box VI-4 below).

Box VI-4. Modus Operandi in Toolkit Development

What are some of the major considerations and parameters involved, and outcomes to be expected from, the suggested approach in toolkit development and application?

One, there are several ready-made toolkit elements and modules which can be collected, combined, reconfigured, adapted and pre-tested for local application. The most flexible toolkits are of a modular nature. The number of constituent modules or elements varies with the complexity and comprehensiveness of each toolkit package, or with the specific subject(s) or purpose(s) they are designed to address or to serve.

In the above context, there is often some overlap -- e.g., productivity enhancement efforts will also require suitable changes in quality control, and in the production and marketing processes. The modular nature greatly facilitates the construction of toolkit packages involving cross-cutting processes and applications.

Two, a three-person team should normally be involved in the whole process of toolkit package development. Team members must have the appropriate skills and experiences – especially in business and financial management, process and product engineering and development, quality control and assurance, packaging and marketing.

Three, the toolkit development process itself would take between 3 to 6 months for completion and pre-testing. Team members will thus be qualified to serve as orientation trainers and application advisers for their own toolkits to the SMEs concerned. Again, the establishment and composition of ASEAN toolkit developers are best undertaken as a joint public-private sector initiative, with overseas collaboration (including from dialogue partners and organizations) as appropriate.

Four, a number of toolkit packages can be first developed within ASEAN-6 at the initial stages of a region-wide programme. Development teams from these countries can then assist SMEs in ASEAN-4 in the application of completed toolkit packages. In addition, they can also collaborate with ASEAN-4 toolkit teams in the development of regional or subregional packages for other substantive areas or purposes. Toolkit programme implementation thus will proceed from the ASEAN regional to subregional and national levels.

Five, some 50 top-level SMEs can be involved, and effectively backstopped, in each toolkit application cycle. The whole process involves (pre-application) orientation training (of some 2 days), self-reliant diagnosis and trouble shooting (1 to 3 months), and post-application exchanges of experiences (1 to 2 days). All these will culminate in the development of business plans or project proposals for future upgrading, technical assistance, or additional self-testing of the SMEs concerned in the immediate future (6 to 12 months).

2. Pilot project in system package development

Again, there is a great scope for collaboration with ASEAN dialogue partners and organizations. China and possibly India, in particular, will be interested in co-operating with as well as in contributing to the joint development of selective toolkit packages for self-reliant applications by SMEs, among other firms.

A pilot project for the development of specific toolkit packages can thus be initiated for the above purpose. As pointed out in the previous discussions (Chapters Four and Five), competitive advantage in the domestic and external markets depends on continuous improvements in product quality, cost and delivery punctuality.

Such improvements, in turn, depend on the implementation of many small (incremental) innovations in products, processes, management systems, and organizational linkages and (inter-firm) networking. Toolkit packages may thus be developed and field-tested to identify the possible sources of value creation, and the changes to be made for their realization, within the enterprises concerned (see Box VI-5 below).

Box VI-5. Areas for Focus in Pilot Toolkit Development

1. Quality certification

There are several industry-specific standards for conformance by suppliers and subcontractors. In particular, ISO quality certification, is no longer an option under the new development context. Two issues should be noted in this connection.

Firstly, there is the high cost of investment in such certification. This is basically due to the high degree of formalization and documentation involved from (third-party) accreditation bodies.

Secondly, the certification process may require a year or more for advance preparations and adoption by the typical SMEs. Such a long gestation period may also entail some protracted disruptions to current operations.

All these constitute an important factor inhibiting the adoption of ISO 9000 (2000) standards of quality management systems in many enterprises (both large and small). However, the burden in cost and time can be significantly lightened through a self-reliant preparatory approach.

2. Productivity enhancement

Likewise, on-going gains in quality, cost and delivery are also not an option under the new development context. Such productivity uplift represents a combination of good or superior practices in several critical areas and parameters.

One relates to the application and utilization of new or innovative technologies in production and management. In particular, just-in time delivery systems, leadership by example, open management are among the soft technologies which help save idle time, shorten cycle time, speed up setup time, and increase employees' productivity and satisfaction.

Two concerns new or innovative ways to prepare material inputs and to organize workflows. The former includes in pre-mixing and pre-sorting, standard sizing, transformation and substitution,

recycling and re-use of materials and parts and so on. Meanwhile, workflows can be sped up through ensuring economic lot sizes, modularization and segmentation, cellular layout, line balancing etc.

Three is embodied in the adoption of new or innovative measures to enhance the effectiveness and efficiency of workers. Among those measures are safety practices and accident prevention efforts, ergo-aides, color coding, error-proofing mechanisms, performance-based incentives, small-group team activities, productivity and quality improvement circles and so on.

IV. Benchmarking SME capabilities and competitiveness

As pointed out in Chapters Two and Five, it is both pressing and self-evident that up-to-date and comparable data and information be collected. Among other things, this is necessary for the monitoring, assessment and benchmarking of the evolving capabilities and competitiveness of SME. A sample survey to address the current absence of such data and information is proposed below.

A. Context and justification

The survey framework is underpinned by three major points of reference. Firstly, there are the CCI and GCI, and their constituent survey questionnaires, from WEF. Secondly, there are the common guidelines, parameters and prerequisites which must be available or operational so as to foster SME sector development and integration. Many of them are discussed at length in the literature on SMEs.[56]

The third reference point is various SMEs-related surveys and questions available in, or reported by, several sources – such as Hall (2002: 57-66), Momaya (2001: 142-152), Tambunan (2000: 95-109), and UNCTAD (1998: 188-195). However, these surveys and questionnaires are both shorter in length and more limited in scope than the assessment framework being proposed below (see Box VI-6 below).

[56] See, for example, Minoza-Gatchalian (2001: 223-236), Raneses (2001:.197-213), Wattanapruttipaisan and Lam (2001: 19-26), Regnier (2000: 150-165), Tambunan (2000: 167-180) and Altenburg (1999: 30-38).

Box VI-6. Foundation of the Survey Framework

Conceptually, SME capabilities and competitiveness can be approximated and grouped under seven categories. The first relates to matters concerning the overall environment in which SMEs operate. The second category portrays the entrepreneurial characteristics which are the driving force of firms concerned, whether they are large businesses or SMEs.

The third and fourth categories cover the extent of current levels of capabilities and competitiveness. They are thus indicative, by and large, of the initial or present conditions and circumstances of the pertinent SMEs. As such, these two categories are an approximation of the CCI of the WEF survey (APMS and HOPDC, 2001).

The fifth category serves as a proxy of the potential of SMEs for quality and productivity upgrading, and for competitive growth. This transformation process is characteristically led by innovation, based on learning and driven by investment. In a way, this category mirrors the GCI which was (newly) introduced by WEF in the Global Competitiveness Report issued in (and from) 2000.

The last two categories of the proposed survey framework deal with matters relating to finance and human resource development (HRD). The importance of the latter grouping has tended to be taken for granted. As evident from the discussion in Chapters Four and Five above, however, HRD has become even more crucial in gaining and sharpening competitiveness, whether for large companies or SMEs.

Some 80 guidelines, parameters and prerequisites can be taken into consideration in designing the above framework for supply-side assessment of SME capabilities and competitiveness. They cover a wide range of matters of importance to the firm.

These matters include the enterprise's orientation in terms of growth, exports and inter-firm networking together with its current approach and linkages to clients and customers. Due focus is also given to the firm's potential of technological upgrading and more flexible production, to financing requirements and access to credit, and to facilities for on-going learning and innovation, whether or not research-based.

The guidelines, parameters and prerequisites (and their proposed grouping into seven different categories) indicated above do not pretend to be exhaustive or exclusive. They are, however, more than adequate for the purpose at hand.

In comparison, for example, the CCI in the WEF report on global competitiveness ranking covers 173 variables which are divided into eight categories. However, this index also extends across subjects which are much broader in both scope and substance than the SME assessment framework under consideration.

In particular, the executive respondents to the WEF survey are posed with such questions as "What is your country's position in technology relative to world leaders?", "Are government programmes successful in promoting the use of ICT?", "Is the judiciary independent from the government and/or parties to the dispute?" and "How common are bribes paid (under various circumstances)?" (Mcarthur and Sachs, 2001: 40 and 46).

As with any statistical exercise, there is certainly room for both revision and fine-tuning of the suggested framework for monitoring, assessment and benchmarking of SME capabilities and competitiveness over time. In this context, another remark on the two WEF global competitiveness indices is pertinent.

The CCI and GCI are well known globally, long established and widely accepted. Nevertheless, they are far from totally solid and vigourous in terms of both the underpinning theory and applied methodology.[57] In addition, there is a host of complex issues which had to be resolved case by case and practical compromises, adopted in compiling the CCI and GCI (Porter, Sachs and Macarthur, 2001; and Lall, 2001).

B. Pilot survey of SME capabilities and competitiveness

To reiterate, a major effort has to be made by government and other stakeholders to build up and maintain an inventory of comprehensive, comparable and up-to-date information and data on SMEs. This is essential for a variety of important reasons -- not least for better policy design, implementation and evaluation, as noted previously.

But the databases can also be set up in terms of specific sectors or industries to provide an objective and systematic indication of the evolving changes (whether progressive or regressive) of SME capabilities and competitiveness within the sectors or industries concerned. Alternatively, they can be grouped for other purposes – such as match-making and partnering activities, readiness for subcontracting or e-commerce, geographical clustering etc.

The survey framework suggested above is a remedial step forward in the right direction. In this context, there is a solid justification for the implementation of a small-scale pilot project for field-testing and fine tuning purposes (see Box VI-7 below).

[57] Lall (2001: 1509-12 and 1515-19) provides a detailed assessment of related theoretical and methodological issues and problems associated with the WEF CCI and GCI; the latter was introduced in its present form from the 2000 report. See also several pertinent references cited in Lall's article. Corruption Perceptions Index, on the other hand, is a "composite" indicator. The 2002 index, for example, was derived from 15 sources of survey results conducted by nine independent institutions. A composite index raises additional difficulties. Lambsdorff (2002) provides a detailed insight into a variety of complex substantive and methodological issues to be dealt with by Transparency International in its (annual) compilation of the index.

Box VI-7. Objectives and Coverage of Pilot Project

The pilot survey will help field-test and refine the sample questionnaire concerning the parameters, guidelines and prerequisites as regards supply-side capabilities and competitiveness of SMEs. It also contributes to the development and fine-tuning of the necessary methodologies, both qualitative and quantitative.

Such a contribution can be seen in two crucial aspects. One relates to the training of interviewers and raters, and the other concerns the scoring and benchmarking of feedback and results from sample surveys and direct interviews.

In addition, when implemented and completed, the pilot project will help to set up workable systems for the formatting, storage, retrieval and utilization of the data and information so collected. This will provide a solid foundation for future surveys as well as for the extension of the number of industries and countries participating in these surveys.

As regards coverage, the pilot project is to survey selectively a small number of SMEs, say, between 50-100 in each member of ASEAN. Preferably these firms are officially registered and have been operating for a minimum number of years (to be specified at the design stage).

The sample sectors or industries are to be limited to a small number (say five) of production activities which are important locally. These activities are likely to range from agro-processing, wood and metal working, standard-technology manufacturing to software development and tourism.

Thus, the sample size for the pilot project ranges from 2,500 to 5,000 respondent SMEs. In comparison, the 1999 CCI was based on about 4022 responses to the WEF Executive Opinion Survey from 59 countries. The number of countries was increased to 75 from the 2001 Survey onwards, involving around 4700 respondents.

It should also be noted that the sample sizes of several well-known surveys are comparative much smaller, within the range of 1000-2000 in number. These surveys include those on Asian economic and political risks, opacity index, African competitiveness report, and corruption in emerging markets. IDM and WEF surveys of global competitiveness are the notable exception with sample sizes amounting to about 3,500-4,700 in number (Lambsdorff, 2002; Lall, 2001: 1515; and Porter, Sachs and Mcarthur, 2001: 16-17).

SMEs-related organizations, as local counterparts within ASEAN, will be requested to collaborate in carrying out the pilot survey. Responses to survey questionnaire are to be obtained on a multi-media basis – involving a combination of mail, telephone, and internet facilities, plus face-to-face discussions. Since this is a pilot project, second-wave interviews (direct or via other media) will be necessary to ensure more complete responses, and greater accuracy and compatibility in their rating.

V. Fostering readiness for subcontracting

The suggested survey above is for monitoring, evaluating and benchmarking SME capabilities and competitiveness on the supply side. The second part of the equation relates to the preconditions and other guidelines for compliance by SMEs. These demand-side requirements are originating from SME clients or partners in domestic or cross-border production networks or supply chains.

A. Context and justification

As discussed in Chapters Four and Five, there are significant collective benefits from domestic clusters of firms, plus those engaged in ancillary or complementary industries and services. Enterprise clustering has, in fact, had a long history in ASEAN and elsewhere. However, this phenomenon has recently received more focused policy attention, in part because of the new possibilities in industrial organization and co-operation bought about by rapid advances in ICTs and transport technologies.

Generally, however, the success record of enterprise clusters is rather mixed in ASEAN, and elsewhere as well (Chapter Five). Many have become dormant or have exhibited limited interactions among the clustered firms. Moreover, demand-driven clusters appear to be more dynamic in terms of productivity gains, knowledge creation and innovation capabilities on a relatively more sustained basis. As such, they resemble more like production network or supply chain arrangements.

By and large, however, a better understanding as well as greater clarity and coherence in the promotion of domestic clusters can be gained from further research. Some of the elements for research focus are presented in Box VI-8 below.

Box VI-8. Issues for Further Research on Enterprise Clustering

- *What are the key drivers of the process of industrial clusters and agglomerations in the national or regional context?*
- *How has the trajectory of (initial) location-specific advantages evolved and how have the new (cluster-based) advantages developed and been exploited?*
- *What are the major push-pull forces in clusters driven largely by demand (external to the cluster themselves), or by producers and their spatial concentration?*
- *How have the roles of focal firms, and those of their suppliers, changed at different stages of clustering (and networking).*
- *What is the nurturing or developmental role of focal firms -- especially in terms of productivity enhancement through the development and transfers of knowledge, technology, and through expertise creation between them and their suppliers?*
- *How have focal firms served as incubators of, as markets for, or as supporters of new business start-ups?*
- *How have new entrants (backward, forward and lateral in nature) been attracted and retained generally?*
- *What is the role of public policy and other support or institutions in cluster formation -- especially in*

the provision of ancillary infrastructure and services?

- *How has the promotion of regional linkages, including through trade and investment liberalization, impacted on the expansion or diversification of clusters, those driven by (external) demand in particular?*
- *Dynamically, what are the major elements of an enabling policy and institutional environment at the higher, or more complex stages, of cluster transformation?*

It was indicated earlier that, as participants in production networks and supply chains, SMEs must comply with wide-ranging preconditions and other requirements. These demand-side prerequisites have also become more exacting over time (see Box VI-9 below).

Box VI-9. Quality, Cost and Delivery: Some Illustrations

1. An external example

On average, a motor vehicle has some 10,000 different parts. Typically, many of them are sourced from all over the world, including from the ASEAN region.

The Ford factory in Toronto, Canada, produces 1,500 Windstar mini vans a day. There are about 800 daily deliveries which should not arrive more than 10 minutes late at any of the 12 different receiving points along the assembly lines.

The supply chain includes about 300 auto parts makers whose production schedules have to be tied to the factory's own computerized assembly systems. In addition, parts must also be loaded into trucks in a pre-arranged sequence to facilitate (and save time) in unloading and assembling.

Transportation of parts is typically outsourced; it is an operation handled largely by SMEs under subcontract. The subcontract for transportation, which is normally fixed for 5 to 7 years, often involves cost reduction of several percentage points a year.

2. A local case in point

In Thailand, a large number of the first-rank suppliers of auto parts and components are independent or joint-venture SMEs. However, most of the parts makers and subcontractors of lower tiers are SMEs.

A defect ratio of less than 100 parts per million (ppm) has long been the norm in terms of product quality requirement. However, the quality stake has been raised to 20 ppm, implying thus zero defect and one hundred per cent quality check on the part of smaller suppliers.

Cost reduction target of 20-30 per cent over the medium term (2 to 3 years) is often demanded from subcontractors. Meanwhile, cost reduction plans and schedules are to be included in documents for supply bidding. The benchmark for cost-reduction exercises is the (free-on-board) prices of similar products on the world market.

As regards just-in-time procurement, the frequency of delivery may be raised from 2 up to 8 times daily for local makers of parts and components. Overseas suppliers of high value-to-weight products are required to make their goods available within 48 hours. The objective is to gradually eliminate inventories altogether at the assembly end.

3. Some observations

Advances in ICTs have made it much easier to manage the supply chain which has become increasingly complex and transnational in nature. Such advances include radio frequency identification and transponders in product packages which can communicate with factories or warehouses.

As a whole, however, continuous gains in quality, cost and delivery depend on factors other than ICTs and transportation technologies alone. There must be on-going improvements in core business competencies. Synergic inter-firm linkages will be equally helpful – particularly in R&D, product and process enhancement, and new market developments.

In that regard, the compliance process requires important changes in mind-set. To begin with, a large number of subcontracting prerequisites are traditionally not practiced or expected by most SMEs, among other firms. There is, for example, little room for compromise on quality and, in this context, compliance to quality management systems recognized worldwide is through certification under the ISO 9000 series of standards (before the revision in 2000), ISO 9001 and 9002 especially.[58]

In fact, such certification is no longer an option for first-tier suppliers and subcontractors. This means that suppliers and subcontractors to companies certified under ISO 9000 series are also expected to be similarly certified. Such an expectation prevails regardless of the tier or rank of their operations within various production networks or value chains.

But significant changes are also required in several other SME business practices. They include meeting certain minimum conditions as regards employment and workers' amenities in the workplace. In particular, a large number of TNCs have become very sensitive and conscious in protecting the image of their brand names. Their inspectors are now sent over the world, including to several countries in ASEAN, to scrutinize and inspect the compliance of their subcontractors and suppliers to a range of ethical sourcing criteria.[59]

Other changes include making regular audits of factory layouts and work flows, offering unconditional product warranties and after sales service, and extending credit on delivered products. There is, moreover, the imposition of penalty clauses for under-

[58] The two are identical except for the exclusion of the design element from ISO 9002. ISO 9001, for example, covers 20 separate system elements relating to design, development, production, installation and servicing. Moreover, certain system elements relating to environmental safety and control have recently been incorporated as part of the revised version of ISO 9001. This is because the ISO 14000 series of standards are not directly concerned with the manufacturing processes. In the field of automotive production, there are the Quality System (QS) 9000 requirements by the Big Three producers of automobile vehicles in the Unites States (namely General Motors, Ford and DaimlerChrysler). QS 9000 is the standard yardstick for all first-tier suppliers to these three automakers worldwide. About two-thirds of the QS 9000 requirements are the same as or similar to those under ISO 9000. The remainder consists of specific quality systems and benchmarks specific to automotive manufacturing. As regards the food and food processing industries, there exist the Quality Systems Regulation (QSR) and the protocols relating to Hazard Analysis Critical Control Point (HACCP). Both sets of standards are internationally accepted and are considered as good benchmarks for quality systems.

[59] Gap (a clothier TNC), Nike, Reebok and so on have been struggling for years to convince their own Western consumers that their high-value products are not sourced from child labour working in an exploitative, "sweat shop" environment. Gap alone has deployed more than 80 inspectors for the purpose. In the past few years, Nike has increased by four times the number of its employees dealing with labour conditions and practices (Murray, 2002: iii; and Kazmin, 2002: iii).

performance, for example, in terms of quality consistency, defect and rework ratios and liabilities, timeliness in delivery etc. (Momoya, 2000: 160-161, and Altenburg, 1999: 32-34).

B. A proposed code of conduct for subcontracting

The process of SME compliance cannot be assessed and tracked adequately at present. Organizationally, there are no schemes for that purpose. Many major TNCs provide assistance to, and monitor the performance of, their own clubs or circles of subcontrators; membership in such clubs and circles is not open for other suppliers or producers, however.[60]

Substantively, the typical or non-negotiable pre-conditions and other requirements for subcontracting have not been complied with or standardized. It is thus proposed below that they are put together for ease of monitoring, especially for the purposes of subcontracting and for match-making more generally.

Indeed, the compiled specifications can serve as general guidelines or "best practices" for emulation and adoption by SMEs. As such, they can form the basis of a subcontracting "compact" or "code of conduct" for gauging the readiness of SMEs for the purpose (see Box VI-10).

[60] A range of financial and non-financial assistance and other promotional measures to enhance quality and productivity are normally made available to their local suppliers by, to mention just a few, Nestle and Motorola in China, Uniliver in India and Viet Nam, Intel in Malaysia, Hewlett Packard in Singapore and Toyota in Thailand. For details, see Wattanaprutipaisan (2002a: 78-82).

Box VI-10. Major Elements in a Subcontracting Compact

1. Quality, cost and delivery

- *Acceptance of, and compliance to, pre-specified standards and guidelines as regards quality, cost and delivery.*
- *Developing methodologies and applying means to ensure continuous improvements in quality, cost and delivery.*
- *Adopting quality management systems and obtaining certification under the ISO 9000 series (especially for exporters and export-oriented subcontractors).*
- *Practicing just-in-time delivery systems and scheduling – including through the maintenance of adequate inventories and their warehousing (at own costs).*

2. After-delivery services

- *Extending credit, and accepting payment after use or after delivery.*
- *Assuming total responsibilities for parts, components, and products -- including the provision on demand of back-up, repair and after-sales services.*
- *Accepting penalties for non-performance and under-performance -- such as in cases of product rejections and defects, and delays in delivery.*

3. Enterprise organization and management

- *Operating ICT systems for real-time, on-line interaction with suppliers (backward) and customers and clients (forwards).*
- *Maintaining in-house systems and facilities for speedy incorporation of new and innovative suggestions, ideas and techniques into product and processes.*
- *Joint participation in R&D programmes (with suppliers, fellow subcontractors and customers) for improved products and production processes, for further product differentiation, and for new product development, testing and marketing.*
- *Ready adoption of basic R&D results for discrete improvements in quality, cost and delivery, and for developing new or additional sources of value.*
- *Commitment to apply the same principles and requirements to secondary and third-rank suppliers of products and providers of services.*

4. HRD and labour relations

- *Provision of facilities for on-going learning in-house, and encouraging skills enrichment activities based on (external) learning and on-site extension activities.*
- *Adoption of "best practices" in workers' skill enhancement and career advancement, and HRD generally.*
- *Maintaining good workers and industrial relations, including the provision of work-place amenities for employers and support for their social welfare.*

5. Periodic monitoring and evaluation

- *Accepting regular checking and audits, by third-parties, of various aspects of enterprise management, organization and production processes.*

- *Encouraging and incorporating, as appropriate, evaluations by both input suppliers and product customers.*
- *Carrying out regular checks and monitoring of the following matters and processes: (i) production lot sizes and lead time, set-up and throughput times; (ii) production defects (e.g., rework, repair and reject ratios); (iii) warranty repair costs and so on; (iv) conditions of the workplace and machinery; (v) schedule of maintenance, repairs and replacement of machinery and buildings; (vi) cleaning, waste disposal and recycling of waste materials; and (vii) lay-out of factory and work flows (including floor painting and color coding and idle time of machinery).*
- *Resolution without undue delay problems and bottlenecks detected by suppliers, clients or customers, third parties, or through own evaluation and monitoring.*

It was proposed earlier that SME capabilities and competitiveness in specific industries be monitored and benchmarked as input for a variety of applications, including for the promotion of inter-firm linkages. Thus, the survey results so obtained on the supply side can be matched against the demand-side prerequisites by TNCs and domestic conglomerates as contained in the subcontracting compact.

The comparison will reveal in a systematic way the extent of supply and demand side convergence for subcontracting and other linkage purposes. Meanwhile, the areas of non-convergence reveal or represent the specific needs for follow-up capacity building and other support services to strengthen SME readiness as subcontractors, or as participants in cross-border production networks and supply chains.

A demonstrated adherence the subcontracting code of conduct will qualify the SMEs concerned as possible supply partners. Such a qualification for subcontracting is just like a certification under the ISO 9000 series does but for total quality control, assurance and management.

VI. ICTs and e-commerce

The major issues are of a Catch-22 nature in most parts of ASEAN at present – namely the low penetration of ICTs in the SME sector itself and, on the other hand, the limited usage of e-business by enterprises, including both customers and suppliers themselves. However, comparable data and information are not available because of the absence of regular surveys on the pertinent matters and issues, especially those of primary concern of and interest to SMEs.

A. Context and justification

Generally, the highly limited reliance on ICTs and e-commerce by business firm, including those within the SME sector, reflects several deeper problems in many parts of the region. The first problem is the lack of trust and confidence on the part of suppliers and customers which itself is due, in a large part, to an inadequate supply of soft infrastructure, legal and regulatory elements especially.

Matters of great importance to business enterprises include (1) the security of e-transactions; (2) the availability of low-cost and reliable payment modalities; (3) effective and efficient delivery and distribution systems; and (4) speedy and inexpensive e-contract enforcement and other (alternative) dispute settlement mechanisms for the resolution of legal and liability issues.

The complexity of such issues is greatly compounded with cross border e-transactions. Faster and reliable delivery is often expected with E-transactions. Weaknesses within the supply chain (e.g., costly, unreliable or time-consuming postal and other delivery services) will certainly inhibit e-commerce. The availability and reliability of product specifications on-line is another issue.

Likewise, secure systems for payments have been developed but, again, these must be applicable to the needs and infrastructure of developing countries, and not just of developed countries only. By and large, therefore, significant efforts will have to be made by both the public and private sectors to create, regulate, stabilize and legitimize the domestic (hard and soft) infrastructure (legal, financial, logistical etc.) and markets (both input and output) for e-business.

The second problem is that ICT infrastructure and facilities themselves are simply inadequate in many parts of the regions (Table V-1 in Chapter Five). Where available, there are often constraints as regards quality, reliability and affordability and accessibility, especially for SMEs in lower income countries. In particular, ICT connection fees and the charges by Internet service providers (ISPs) are often comparatively high. Besides, ISP access points are limited and there are often considerable delays in accessing internet services.

The third problem relates to cost-benefit considerations (or returns on investment). Generally, the costs of basic equipment and its maintenance constitute another heavy burden on many SMEs (except the tiny proportion of enterprises in the top layers). The proposed duty-free trade in ICT equipment and components within ASEAN is thus a helpful step in the right direction.[61] So are efforts to manufacture and design low-cost and "dedicated" computers and software for e-business, among other purposes.

The fourth problem is that "wiring" and hardware alone are never enough. Other push-pull factors in the penetration of ICTs and e-commerce within the SME sector include the availability of a wide range of specific or custom-made software of suitable quality, and at affordable cost in time and money. Such a supply has not always been the case, however.

The fifth problem concerns the limited knowledge, awareness and skills on the part of SMEs concerning the promise and requirements of ICTs as well as e-business. As in the case of subcontracting arrangements and compact (see Box VI-10), the adoption of e-commerce will entail basic changes and shifts in business strategies, operations and technologies. Many

[61] Notably in the case of China, for example, tariffs on information technology products (including computers, telecommunications equipment and semiconductors) will go down from an average rate of 13.3 per cent on WTO accession to zero by 2005. There are plans in India for the mass production of low-cost computers for specific applications.

of these changes are inherent or implicit in the discussion on ICT and e-transaction requirements above.

B. Five proposals on e-trade for SMEs

Multi-dimensional capacity and infrastructure building is needed at the national and regional levels; and so are resource mobilization and priorities setting. This is an on-going prerequisite, and the e-ASEAN Framework Agreement (signed in 25th November 2000) is another laudable achievement and ambitious endeavour in regional co-operation and facilitation.

But specific skills and capabilities relating to ICTs or to e-commerce will also have to be established and upgraded over time within the SME sector in the region. This need highlights, among other things, the relevance and importance of self-reliant toolkit packages for problem diagnosis and capacity building by the SMEs themselves -- as discussed in Chapter Two and Five, and proposed in Chapter Six.

A number of transitional or short-term measures can be suggested to foster the gradual penetration of ICTs and e-commerce within the SME sector (see Box VI-11 below). The implementation of these proposals, which vary in complexity and organizational requirements, will benefit greatly from co-operation and facilitation within ASEAN, and with ASEAN dialogue partners and organizations as well.

Box VI-11. Stop-gap Measures for E-commerce Promotion among SMEs

One, a survey can be carried out to gauge the extent of ICT usage and e-commerce penetration, and hence of related needs technical and other assistance. It can focus on selected SMEs in the top segments of various priority industries and sectors. These segments are the primary target beneficiaries of the proposed policy blueprint, as explained earlier (Chapter Two).

Two, the public and private sectors can jointly set up and maintain a register of SMEs which are ready to engage in e-commerce as well as to guarantee their on-line products. The results obtained from the ICT and E-trade survey (suggested earlier) will facilitate the "registering" or accreditation process. In addition, the survey questionnaire itself will provide some objective and systematic parameters and benchmarks for the (sectoral) classification and e-trade accreditation of the SMEs concerned.

Three, it will be useful to have regular meetings within ASEAN and with dialogue partners and organizations. This is to exchange views and policy experiences as well as to identify areas of co-operation in the promotion of domestic and external e-trade.

Such meetings can help disseminate more widely success stories and best practices as regards the adoption of ICT-based transactions and e-commerce by business firms, in particular SMEs, from within and outside the region. Preferably, the process has to be complemented with the parallel distribution of toolkits, guidebooks and user manuals. The self-reliant packages so supplied in a multi-media format will greatly facilitate familiarization activities by SMEs in the uses and applications of the pertinent hardware and software.

Four, there is justification for the establishment of ICT-based, interlinked

networks of provincial, regional or industry-wide clearing houses for SMEs. Such an initiative is best jointly undertaken by the public and private sectors -- including SME or industry associations, and civil society organizations as well.

These on-line networks will help to advertise the available products from various groups of SMEs on the supply side. As such, they can facilitate the "matching" of products or businesses. Additionally, they can also serve as regional or subregional trading points for e-transactions between businesses, or between business government agencies or consumers.

On the demand side, these networks may be tasked with the collection, storage, up-dating and dissemination, regularly or on specific request, of a high-quality information on subjects of interest to SMEs. These subjects may include opportunities for e-trade, for technology transfers and upgrading, for inter-firm networking and alliances and so on.

Five, in measured and gradual steps, the public sector may make greater use of e-commerce and e-documentation in the procurement of materials and other inputs. This can act as a positive force in fostering the gradual adoption of e-business by domestic buyers as well as suppliers.

VII. Finance

As in the case of telecommunications infrastructure, SME financing problems have also to be seen against a more general context – namely that development finance is in short supply virtually in all developing countries. Thus, in one form or another, financing problems and the associated priorities setting will remain to be dealt with during the successive stages of socio-economic development over time.

A. Context and justification

Nevertheless, it is also clear that financial intermediation in support of SME sector development and integration can be much improved on both the demand and supply sides. Such on-going enhancement constitutes another integral part of the financial (and economic) development process itself. There are neither quick fixes, nor sustainable alternatives or options.

Four common denominators can be identified as regards SME financing issues. Firstly, on the funding demand side, SMEs in the top layers of their own industries or sectors must have, or must be assisted to have, standardized and generally acceptable accounting and financial information and reporting systems. This can be achieved through the toolkit package approach, among other modalities (see Box VI-12 below).

Box VI-12. Uses and Abuses of Financial Information Disclosure

Adequate disclosure of useful information is necessary to present, in a fair and transparent manner, the financial health and track record (or the credit footprint) of the concerned enterprises over time. Actual or perceived deficiencies in disclosure are attributable directly to the lack of due enforcement. It can also be due to a persistent disregard for, or non-adherence to, existing and accepted standards and norms in accounting and auditing.

Proper disclosure constitutes an indispensable input for the process of due diligence on the institutional supply side as well as for the preparation of a bankable business plan on the financing demand side (more below). But financial and accounting information is also useful for other purposes, including for diagnosis of possible problems or hidden advantages.

Financial statements from an SME, for example, may reveal a low debt-to-equity ratio. In this case, either management is highly conservative or the benefits of leverage may not have been appreciated.

On the other hand, operational expenditure may be relatively higher than the norm among business firms in the same industry. This may have some implications (for remedial purposes) regarding the inadequate levels of operational efficiency and effectiveness of the SME concerned -- especially in the combination and utilization of inputs, or in technological application and upgrading.

The second common denominator is that SMEs (those in the top layers in particular) must have, or must be encouraged and assisted to have, better and more effective communication with financing institutions and financial providers. This takes the form of a business plan in cases where these institutions and suppliers are approached for funding purposes. Collateral requirements will be less stringent if loan financing is based largely on the commercial feasibility of a proposed project.

The third common denominator in SME financing issues relates to the (institutional) financial supply side. There are elaborate systems for credit rating or credit scoring in all developed countries. These have rendered the process of loan evaluation and approval more objective and systematic; and less time consuming and costly on both parties in those countries.[62]

However, the processes and systems for credit rating and scoring are relatively less sophisticated and less extensive in many ASEAN member countries. This is due partly to the lack of information for referral purposes (more below), and partly to the lack of consistent and comparable information. There is inadequate expertise in asset evaluation and project appraisal within the formal financial sector as well. All these weaknesses contributed their share to the 1997-1998 financial and economic crisis in East and South-East Asia.

The second direction is to build up credit information and referral systems to backstop and underpin credit rating or scoring services. These systems constitute simply another prerequisite in economies which are becoming more sophisticated and diversified, such as those in the middle or upper-middle income range. But they, too, have to be built up gradually in other economies, and this widens even further the scope for regional co-operation.

[62] As can be seen from recent incidences, well-developed credit rating or scoring facilities and credit information and referral systems will not eliminate loan defaults. However, their systematic and objective operations will minimize greatly the incidence of non-repayments and loan delinquencies. This is because loan defaulters and other bad credit cases will be "on-screen" and can thus be easily identified and spotted in the loan assessment and approval process.

Clearly, the capacity-building efforts on the institutional financial supply side are of a medium to long-term nature. They call for judicious partnership between the public and private sectors, and with external collaboration as well. As is also the practice elsewhere, some components of the systems (e.g., credit information reference and referral services) can be set up and operated by third parties to minimize conflicts of interest.

B. Four proposals to facilitate SME financing

The following proposals are made because there are few, if any, viable options in the long run. Their importance to SMEs will also increase as the domestic economies develop and integrate regionally and globally in the coming decade. However, there are systemic issues in some of the proposals and, as such; the possible difficulties cannot be underestimated. These problems (on both the demand and supply sides) must be addressed as a matter of policy necessity, and not of choice.

1. SME financial information disclosure

The data and information for disclosure have to be useful in terms of reliability, relevance, compatibility and understandability. Standard (international) accounting rules and norms already contain sufficient disclosure to meet those criteria. By and large, therefore, the required financial data and information are not that extensive or onerous, particularly to the SMEs in the top layers of their own industries and sectors.

As can be seen in Box VI-13 below, the main elements in bank assessment of credit risk internal to the firms itself are largely available from standard statements of accounts and basic information (both financial and production in nature) from the firm. There may be more detailed analysis for credit rating purposes (point 3 in the Box) but again the required data and information can be provided without much difficulty by many SMEs, provided that a good record is kept by them.

Box VI-13. Factors for Considerations in Credit Risk Assessment

1. External risks. *Normally, the extent of credit worthiness is rated on criteria both external and internal to the firm itself. Among the external, systemic and market-related risks are:*

- *Nature of the industry or market concerned.*
- *Relative size and current structure of the same industry or market.*
- *Loan default and bankruptcy rates in the industry or market concerned*
- *Dominant or concentration ratios in complementary or supporting industry or market.*
- *Exposure to, and linkages with foreign market forces (on both the supply and demand sides).*

2. Enterprise-specific risks. *Assessment criteria internal to the firm include the following parameters, with the first two typically being given almost one-half of the total weighing involving six parameters.*

- *Record of profitability, such as returns to assets and shareholders' capital (if already in operation) and/or business plan documents.*
- *Capital and ownership structure.*
- *Liquidity and cash flows, and retained earnings.*
- *Size.*
- *Growth history.*
- *Activities*

3. Other parameters. *Additional considerations in credit rating and loan appraisal process include such factors as:*

- *Asset structure, growth and change.*
- *Liabilities structure, growth and change.*
- *Structure of assets relative to income structure*
- *Current liabilities to net assets.*
- *Net worth to total interest expenses.*
- *Operating profits to total assets*
- *Liabilities over growth of net worth.*
- *Total liabilities (less cash on hand and marketable securities) to total assets.*
- *Retained earnings to current liabilities.*
- *Cash on hand and marketable securities to total assets.*
- *Real total assets.*

Thus, priority should be given to the development and distribution of toolkits packages specifically dedicated to financial accounting, and to record keeping and reporting. These packages can be supplemented by short training courses which can be convened by public and/or private sector bodies and which can involve various degrees of cost sharing, as appropriate. In any case, the training costs will not be excessive because of the generic nature of the subjects, and the large number of interested SME participants.

2. Business plan preparations by SMEs

Basically, a business plan is also generic (or universal) in nature and structure (see Box VII-14 below). The same dedicated toolkit approach, as suggested for financial accounting and information reporting, can also be recommended to assist SMEs in their business plan preparations. Indeed, it is particularly suitable for a "dehydrated" business plan which normally is only 4-10 pages in length.

Box VI-14. Typical Structure of a Business Plan

A bankable business plan may run to hundreds of pages, depending on the scope and technical complexity of the proposed business activity or service. Generally, it has the following structure.

- *Executive summary.*
- *Brief history and main characteristics of the industry concerned.*
- *History of the company and its products, including mission statement and business philosophy.*
- *Market research on the proposed product or service, and SWOT analysis (strengths, weaknesses, opportunities and threats).*
- *The economic and financial aspects of the proposed business product or service.*
- *The marketing plan.*
- *Design and development plans.*
- *Manufacturing and operations plans.*
- *Management team -- including structure and personal profiles of the principal executives and managers, their responsibilities and targeted achievements.*
- *Overall planning and production schedules.*
- *Critical risks, problems and assumptions.*
- *The financial plan.*
- *Proposed company stock offering or ownership equity structure, and*
- *Attachments and appendices.*

A dehydrated business plan is required for initial or exploratory funding discussions with potential investors or financiers. It covers keys aspects of the proposed business activity or service. It can be drawn up largely within the firm on the basis of the relevant toolkits and guidebooks, supplemented by some extension activities and consultation services as necessary.

However, the preparation of a (full dress) business plan is a more complicated and often time-consuming exercise (see Box VI-14 above). A large number of details and estimates will have to be given on a wide range of subject matters – from market surveys and projections regarding the particular industry or sector, development and operations plans, to management and financing issues.[63]

[63] Timmons (1990: 377-397) contains details of a typical business plan along with a practical exercise for illustrative purposes. Generally, the executive summary of such a plan provides (a) a description of the business concept or of the business itself; (b) the opportunity and strategy; (c) the target market and projection;

In addition to the toolkit packages, BDS and extension activities are necessary in the preparation of a fully bankable business plan for many SMEs. Their additional needs in this process can be provided on a commercial or semi-commercial basis.

Alternatively, the financial institutions concerned can also provide advice and assistance to ease and speed up the lending process itself. The provision of such advice and assistance can be justified as an integral part of institutional efforts made to support SMEs and, on the other hand, to ensure due diligence and prudential practices on the part of the lending institutions themselves.

3. Institutional credit rating and information systems

From the earlier discussion, it is clear that a parallel effort has to be made on the institutional supply side as well. Firstly, the capabilities of financial sector institutions to define potential credit risks have to be developed and/or strengthened. Since lending functions are spread through out an organization, systems must be in place to better monitor (institution-wide) adherence to established procedures and guidelines, including those relating to due diligence and lending prudence.

The main parameters in credit risk rating are noted in Box VI-13 above. Back-up facilities are also needed in the credit appraisal process and thus, there is the second (or supplementary) requirement for credit information systems for reference or referral purposes (see Box V-15 below). The systems can be set up in-house, as indicated previously. They can also be operated by third parties to minimize conflicts of interest, and to maximize objectivity and accountability.

(d) the comparative and competitive advantage; (e) the team; and (f) the stock offering. Market research and analysis may include (a) potential customers; (b) market size and trends; (c) current competition and potential new entries; (d) estimated gains in market shares and sales; and (e) on-going market evaluation. The marketing plan has to cover such parameters as (a) overall marketing strategy; (b) pricing; (c) sales tactics; (d) service and warranty policies; (e) advertising and promotion; and (f) distribution.

The next part of the business plan is normally devoted to production and productivity issues. The product design and development plan contains (a) development status, phases and tasks; (b) estimated difficulties and risks; (c) product improvements and differentiation; (d) costs; and (d) licensing and other proprietary matters. The manufacturing and operations plan provides information on (a) the operating cycle; (b) geographical location; (c) input suppliers and subcontractors; (d) utilities and facilities requirements; (e) equipment and buildings, and their scheduled improvements and maintenance; (f) manufacturing strategies and plans; and (g) regulatory and legal issues.

Another part of the business plan deals with management and financial matters. The management plan gives details concerning (a) the organization chart; (b) key management personnel; (c) management compensation and ownership; (d) ownership structure and investors; (e) employment contract terms, and other agreements as regards stock options and bonuses; (f) board of directors; (g) shareholders rights and restrictions; and (h) outside professional advisors for support services. The financial plan contains (a) actual income statements and balance sheets; (b) proforma or estimated income statements and balance sheets; (c) proforma or estimated cash flow analysis; (d) breakeven charts and calculations; and (e) financial highlights. The proposed company offering deals with matters relating to (a) the desired structure and terms of financing; (b) offering sequence and details; (c) capitalization details; (d) proposed uses of funds; and (e) estimated investment returns.

Box VI-15. Main Elements of a Credit Information File

Again, the information contents are not that demanding institutionally. The following items are normally required:

- *Borrower names and contact addresses.*
- *Lines of business or industries or sectors.*
- *Date of credit or overdraft approval.*
- *Uses of the disbursed loans and overdrafts.*
- *Loan maturity date, amount, interest rates (and currency denomination).*
- *Principal sources and amounts of repayments*
- *Nature and value of collateral or security (on a valuation basis in the case of fixed assets)*
- *Total outstanding liabilities, including principal and interest due.*
- *Estimated real and contingent liabilities in case the institutional lender is absorbing the credit risk.*
- *Record of delinquency, arrears or non-repayments, if any.*
- *Brief description of the monitoring activities carried out (within the organization) for the loans or overdrafts*
- *Borrowers' related financial information, including current financial statements and other pertinent information.*
- *Notes on sources and uses of outside credit information reference or referral services concerning borrowers.*

The above two requirements on the supply side are systemic in nature and as the credit rating (or scoring) processes and credit information systems are applicable to all financial sector customers or clients. However, the special needs and circumstances of SMEs should also be adequately featured in the pertinent systems and processes. As such, staff competence in SME credit origination, appraisal, supervision and monitoring, and the related reference and referral processes, should be a matter for special attention and on-going enhancement, particularly within banking institutions.

Furthermore, several larger systemic issues are to be resolved in the context of SME financing. As indicated briefly in Boxes V-8 and 9 (in Chapter Five), these include the adequacy of capitalization by government or donors, especially in credit guarantee and venture capital schemes.

There are also issues concerning managerial professionalism and initiatives in running the various financial schemes. Moreover, greater objectivity and transparency are needed in the appraisal of credit worthiness and fixed assets, or of the feasibility and potential success of proposed business projects.

Furthermore, efforts must be made to widen and deepen continuously investor interest, especially in the mobilization of venture capital, and to ensure the systematic accreditation of inventory quality and their warehouse receipts; the latter should preferably be tradable. A medium- to long-term measure in several ASEAN countries is the establishment of domestic capital markets (in equity and bond issues and trade) for SMEs (discussed previously in Chapter Five).

SME credit rating and credit information systems can be regarded as essentially a national or country-specific initiative. However, given the current diversity in development, elements of regionality and regional integration can be identified.

Generally, there is a great scope for periodic exchange of views and policy experiences as well as capacity building within ASEAN. Moreover, the same process is equally applicable between ASEAN and its dialogue partners and organizations. The agenda and parameters for collective interaction and collaboration can deal with some or all of the issues raised above, or raised in connection with SME credit rating and credit information systems.

4. Regionalization of financial resources and information

The same elements of regionality and regional integration also feature in the above matter. Again, China is likely to be an interested participant in the process.

The pooling of existing financial resources and financing services -- such as credit guarantee schemes, venture capital funds, inventory financing (or factoring) arrangements – are among the many other options for widening and deepening the financing and investor base for SMEs. Indeed, under certian conditions, national or industry-specific databases can also be regionalized to facilitate inter-firm linkage integration efforts (involving SMEs) at the ASEAN regional or subregional levels.

The regionalization of resources and information (including those of a financial and technological nature) is likely to be of a medium- to long-term nature. There are a host of systemic issues and difficulties to be resolved and harmonized in the process. Meanwhile, however, a few feasible first steps and workable examples can be considered.

It was noted earlier in Chapter Five that the Republic of Korea has one of the largest SME credit guarantee scheme among developing countries. The outstanding balance of guarantees amounted to over US$ 28.3 billion as of June 2000. What is more, the scheme is backed up by a relatively elaborate and sophisticated system of credit rating and credit worthiness assessment.

The system has brought in substantial earnings from its rating of domestic applications for guarantees. But credit rating services have also been carried out on outside or non-Korean firms wishing to do business in the Republic of Korea, or to enter into inter-firm relationships and alliances with Korean enterprises (Levitsky, 2000: 132).

Clearly, much can be gained by ASEAN from the experiences of the Republic of Korea and, for that matter, of Japan and other ASEAN dialogue partners. Some of the main items in the agenda for such collective interactions have been discussed previously (see Boxes V-8 and 9 in Chapter V, and VI-14 through 16 above).

VIII. Conducive policy environment

Generally, the policy framework on SMEs is essentially a national or country-specific matter. Nevertheless, many elements of such a framework again lend themselves to intra- and extra-regional interaction and co-operation -- especially given the current diversity in development, and hence in needs and capabilities within ASEAN.

A. Context and justification

A conducive environment has to exhibit a reasonable degree of consistency, coherence and clarity in the policy, regulatory and institutional framework at the macro, sectoral and microeconomic levels. These prerequisites serve to minimize the unexpected constraints on, and unintended biases against, the SME sector. They also exert a positive, mutually reinforcing (rather than counter-productive) impact at various levels and layers of the domestic economy (see Chapter Five).

Secondly, such an environment embodies better fine-tuning of policies, more judicious sequencing of policy changes, and greater transparency and accountability in policy implementation. All these help, in turn, to minimize the dislocations which are inevitable at various transitional stages. They also help speed up the adjustment and re-engineering processes (whether positive or defensive) for SMEs.

Thirdly, within the public sector itself, there has to be greater synergies among, as well as better coordination of, the large number of programmes and projects in support of SME sector development and integration. It is also necessary to have periodic evaluation of the impact of delivered programmes and projects. Matters relating to performance management are discussed at length in Chapter VII of the proposed policy blueprint.

Fourthly, there must be greater coordination and synergies between government and the private sector, including in the provision of BDS and extension activities for SME capacity building and strengthening. The principle of subsidiarity is pertinent in this regard (see Box VI-16 below).

As was clarified earlier, however, there are weak or dysfunctional market mechanisms, and very limited or elementary BDS from the private sector in several countries within ASEAN. Despite their blemishes (Chapters Two and Five), public-sector agencies may thus have to assume a primary function, with external assistance as necessary, in providing SMEs with BDS and extension activities until private capabilities are sufficiently developed, diversified, relevant, accessible and affordable.

Box VI-16. Rational Division of Efforts in the Provision of Business Development Services

***1. Government provision**. Generally, BDS should come largely from the public sector if the services concerned have these characteristics. One, they are generic in nature. Two, they are largely external to the target beneficiaries. Three they can generate important externalities in the delivery process. Four, they are supplied in a collective manner. Lastly, they tend to be inexpensive on the average and at the margin (that is relative to the large number of recipients).*

BDS which belong to this category include:

- *Training in entrepreneurship development.*
- *Management skill training (quality standardization and control, management of technologies and human resources, product design and development, strategic business planning, negotiating joint ventures, pre-feasibility study and business plan preparations, management of change etc.).*
- *Business short courses – including packaging and marketing, inventory control, export readiness, trade documentation, e-commerce documentation, machinery and factory maintenance etc.*
- *Vocation training, and remedial and advanced re-training.*
- *Dissemination of information on trade, markets and technologies etc.*
- *Trade and investment forums etc.*
- *Accident prevention and safety best practices.*

***2. Semi-public provision.** BDS should, by and large, come from semi-public and industry or trade associations if the services involved are industry- or sector-specific. In addition, they can be more sophisticated in nature – thus involving higher supply costs to clients. On the other hand, there is greater flexibility in the delivery of such services.*

BDS which belong to this category include:

- *Surveys on industry outlook and business opportunities.*
- *Trade fairs and product exhibitions, business guides and handbooks.*
- *Study/factory visits.*
- *Entrepreneur exchanges and internship schemes.*
- *Domestic and cross-border inter-firm networking and match-making.*
- *Industry/sector forums and websites. Advice on market, technology and R&D, quality control and assurance, finance and personnel*
- *Upgrading and restructuring etc.*

***3. Private provision.** BDS provision should come mainly from the private sector if the services concerned are enterprise-specific and/or tailor made to the particular needs of the recipients. As such, the supplied services tend to be higher in quality and/or more costly. They are also more demand-driven in nature.*

BDS which belong to this category include:

- *Selection of machinery and choice of production techniques (e.g., lot size, set-up time and throughput time, lead time etc.).*
- *Plant layout and work flows, input sourcing and inventory systems*

(floor painting, color coding, cleaning and waste recycling etc.).
- *Scheduling of maintenance, repairs and upgrading.*
- *Product enhancement and product-specific improvement in productivity.*
- *Diversification of input/output mix.*
- *Improvement in sourcing and storage, in advance preparation, application, and in substitution of inputs.*
- *Industrial management and audits.*
- *Market surveys and testing of specific products.*
- *Advertising and promotion.*
- *Credit and financing.*
- *Equipment leasing and inventory financing.*
- *Documentation for imports and exports.*
- *Customized e-commerce and e-trade documentation.*
- *Accountancy and auditing, and taxation and legal services.*
- *Workers relations and welfare etc.*

B. Seven proposed functions for policy consideration

Government activities and services in support of SME sector development and integration have taken different institutional and organization forms. Some are delivered by public-sector agencies while other are operated as part of a Ministry or Ministerial Office.

A one-stop agency for the promotion of SME development would be helpful, just like its counterpart in the promotion of foreign direct investment. The establishment of such an agency serves to conserve scarce resources, both financial and human, within the public sector; this is an important consideration in an environment of "leaner and meaner" government (Chapter Two). It will also help minimize inter-agency problems and conflicts (Chapter Five).

Such an agency also embodies the horizontal aspect of the subsidiarity principle – namely the synergic division of labour among bodies and institutions within the public sector itself. A synergic partnership between the public and private sectors in the provision of BDS for SMEs, discussed earlier (see Box VI-16 above), represents the vertical aspect of the principle.

Some major functions which are best delivered or coordinated by a one-stop agency in support of SMEs are outlined in Box VI-17 below. These functions encompass many activities of both a domestic, subregional and international nature.

Box VI-17. Some Functions of a One-stop SME-support Agency

1. Facilitation

- *Registration of SMEs – a process currently requiring much simplification and streamlining on a coordinated basis (Chapter Five).*
- *Fostering more effective representation of SMEs in public-private sector dialogues and exchanges of views as inputs for mutual consideration.*
- *Encouraging SME participation in product exhibitions and trade fairs.*
- *Serving as broker or facilitator of the trading and distribution of SME goods and services.*

2. Monitoring and evaluation

- *Monitoring selected policies, programmes and projects relating to SMEs to ensure adequate consistency, coherence, clarity and transparency in objectives, and in expected impact and outcomes.*
- *Assisting in, and monitoring, the coordinated implementation of selected SME support policies, programmes and projects.*
- *Carrying out periodic evaluation of the impact and performance of selected policies programmes and projects in support of SMEs.*
- *Monitoring SME-related credit and financing programmes in the banking sector so as to identify for policy action constraints and bottlenecks on supply and demand sides.*

3. Outreach

- *Making periodic surveys to evaluate and benchmark the capabilities and competitiveness of selected SMEs in priority industries and sectors.*
- *Monitoring the subcontracting compact, and maintaining a register of SMEs' compliance to the compact or readiness for subcontracting.*
- *Developing a range of toolkit packages for self-reliant capacity building by SMEs – including those on accounting, financial and business planning and reporting.*
- *Conducting training courses on entrepreneurship development, and assisting in the monitoring of trainee entrepreneurs' post-training progress and problems.*
- *Serving as an information center and clearing house – including on BDS, technologies and e-commerce.*

4. Advocacy

- *Dissemination of high-quality information on domestic clustering of firms and supportive industries.*
- *Dissemination of high-quality information on inter-firm linkages and collaboration within and across borders.*
- *Dissemination of success stories, and good or superior practices of SMEs within and outside ASEAN – with special reference to e-commerce, product and process innovation in priority industries, and new and innovative financing modalities.*
- *Organization of study visits to, and internship schemes in, domestic and external firms for SMEs.*
- *Convening meetings of domestic and international participants on SME-related issues and development trends*

5. Research

- *Conducting policy-based and action-oriented research on SME-related issues and development trends.*
- *Dissemination of regional and global research results on SME-related issues and development trends.*
- *Maintaining a roster of experts and skilled professionals in various fields to backstop other function noted above.*

6. Information systems

- *Setting up and maintaining various databases on SMEs – including those classified according to priority sectors, capabilities and competitiveness, readiness for subcontracting, e-commerce activities, participation in clusters and networks of firms etc.*

7. Liaisons

- *Maintaining contact and sustaining collaboration with domestic, regional and global organizations and institutions, especially those with a mandate on, or interest in, SME development.*
- *Maintaining contact and sustaining collaboration with private-sector bodies and NGOs a mandate on, or interest in, SME development at the domestic, regional and global levels.*

Chapter Seven

MANAGEMENT OF POLICY, PROGRAMME AND PROJECT PERFORMANCE

Contents

The following chapter is complementary to Chapter Six where a wide range of policy measures and options were suggested for the proposed blueprint for the ASDD 2002-2012. It has several objectives and expected outcomes.

I. Overview

The first objective is to explain in non-technical terms the main concepts and steps in the process of results-based management of policies, programmes and projects. The explanations are supplemented with several illustrations as regards the prerequisite information and data for performance management, including the qualitative and/or quantitative measurement and evaluation of such performance.

Thus, the immediate result expected from this chapter is a better awareness and more informed perception of the nature and implications of performance measurement and evaluation. These two processes constitute an integral part of the results-driven management of policy, programme and project performance.

The second objective and expected result are more specific in context. Chapter Six of the proposed blueprint contains a large number of policy suggestions. Many of them can be readily translated, adjusted or incorporated into national and/or regional programmes and projects for implementation in support of SME sector development and integration.

The following chapter provides, therefore, some guidance for programme and project design with a view to facilitating results-based performance management. Indeed, considerations of cost efficiency and implementation effectiveness requires that measurement and evaluation parameters and benchmarks be developed and incorporated and specified right at the design stage of the policies, programmes projects – and not just be tacked on as an after thought.

II. "What gets measured gets managed"

The (simple) sequence of performance relationships proceeds from inputs (financial, technical and human resources) to activities (the organization of seminars or training courses) to outputs (documented reports and recommendations, upgraded skills of,

and more informed perceptions, by trainees etc.). It has its own usefulness -- namely the ease and simplicity of use in the management of policies, programmes and projects.

However, a trade-off from this simple sequence is less precise and inadequate information and data in two important areas (see Box VII-1 below). One relates to the relevance and usefulness of the results (short-term, intermediate and long term) to the target beneficiaries. Two concerns the relationships between these actual results and, on the other hand, the designed objectives of the pertinent policies, programmes and projects.

Furthermore, there is yet another complication. Under the current sequence of activities, there is limited continuity in the monitoring and assessment of (intermediate) outcomes as well as (long-term) impact. The latter includes replication and spill-over effects within and across the intended target groups arising from the implementation of policies, programmes and projects concerned.

Box VII-1. Planning and Implementation Sequences

Programme and Project Planning Sequence
==========>

Objectives	*Results*	*Outputs*	*Activities*	*Inputs*
↕	↑			
Performance evaluation ↔	*Performance measurement*			

<==========
Programme and Project Implementation Sequence

A. General considerations

Policies, programmes and projects are designed and implemented to achieve certain planned and designed objectives which may or may not be totally reflected in the actual results.[64] The latter is the main focus of performance measurement and evaluation.

Results can be concrete and are expressed in specific numbers -- such as quantities and values of production and exports, amounts of profits realized, volumes of workers employed, number of entrepreneurs trained and inter-firm linkages promoted etc. Or they may be intangible -- such as knowledge and skills gained, built-up trust and confidence,

[64] It should be mentioned here again that terminologies relating to business and project planning and performance management adopted and/or understood by different organizations and stakeholders often are not strictly comparable or homogenous. APMS and HOPDC (2002) are updating and enlarging, in a third edition since 1993, *non-technical* explanations of over 250 basic terms commonly found in the preparation and evaluation of business plans and development projects. Earlier versions of this glossary have proved very useful as part of the background documentation or reading materials for seminars and training courses, or for enrichment and refresher training, on the above subject matters. The target participants in such seminar and training activities include SME entrepreneurs and business managers, staff of SME-related agencies and organizations, and public and private-sector officials with responsibilities in various processes and activities relating to business and development project planning and execution. The explanations and illustrations in this glossary are based on, and simplified and expanded from, those contained in World Bank and IMF (2001); UNDP (1997); Commission of the European Communities (1993); Ferrer (1993); Stickney, Weil and Davidson (1991); and Gittinger (1989).

changed and changing mindsets, improvements in the overall environment regarding SME-support policies and institutions etc.

Typically, the actual impact and results of policies, programmes and projects are composite in nature. They embody the convergence of a number of internal and "external" forces and influences. Many of the latter, however, are outside the control and purview of the policy measure, programme element or project under consideration. Indeed, some of these exogenous forces may even offset or reduce the overall number or intensity of the actual impact and results themselves.

Performance information and data thus provide some concrete and comparable indications of plausibility – namely that the accomplishments which have taken place are, to a considerable extent, facilitated or assisted by the implementation of the policy, programme or project activities concerned. With that reservation in mind, the extent and intensity of these impact and achievements can then be measured, gauged and benchmarked quantitatively or qualitatively (see Box VII-2 below).

Box VII-2. Uses and Usefulness of Performance Management

Performance measurement is helpful for other purposes as well. One, as feedbacks, they provide early warnings of problems and prospects -- constituting thus a rational and solid basis for mid-course adjustments, say, in activities programming and budgeting as or when needed.

Two, as impact indicators, they keep in focus the end users plus the intended benefits to them. This helps, in turn, to sustain or enhance the relevance and usefulness of the policy measure, programme element or project under consideration.

Three, as lessons learnt, performance information and data facilitate the process of strategic planning and activity prioritization. They also serve to improve the design and implementation of future or follow-up activities.

And finally, as a public relations exercise, better performance management promotes support from all kinds of stakeholders. These may range from grass-root target beneficiaries, government at various levels and layers, to donor countries and agencies and civil society organizations.

B. Parameters and Benchmarks of Performance Management

But *what* is to be covered in or by performance information and data? In the simple sequence noted earlier (see Box VII-1 above), the performance of policies, programmes or projects is indicated by (and varies positively with) the rate of delivery and the number of delivered outputs in relation to the designed or planned target levels. Thus, the objectives are *implicitly assumed* to have been reached or achieved with the delivery of outputs from the pertinent policy measure, programme element or project.

Follow-up evaluation of the long-term impact and intermediate outcomes is normally not undertaken, or is carried out only in an ad hoc and truncated basis. As such, the interactive relationships between various categories of results and the objectives themselves

are not indicated or measured (whether qualitatively or quantitatively) in any adequate or systematic manner in the above sequence.

Thus, what needs to be assessed is, firstly, how the delivered outputs set the stage for the achievement of the higher-order goals? Secondly, how the attainment of these goals contributes to the final realization of the overall objective of the implemented policies, programmes or projects?

Output delivery may include, for example, the number of trainees and completed training courses on SME entrepreneurship development. Or it may concern the number of distributed toolkits packages for self-reliant SME capacity building on its own or for inter-firm linkage purposes.

However, the intermediate (or mid-term) outcomes and effects from such (immediate) outputs may relate to the widening and deepening of the local entrepreneurship base in selected priority industries. Or they may relate to enhanced capacities in enterprise organization and management, or to the adoption of suitable processes to meet tighter market standards and subcontracting requirements.

Meanwhile, the multi-year impact as well as the ultimate development objective of the implemented activities (that is entrepreneurship training and toolkit distribution) may be *respectively* the emergence and prevalence (or existence) of a culture of SME entrepreneurship, innovation and networking – within the targeted priority industries or sectors, or economy-wide.

Thus, the (intermediate) results constitute the bridge between their (ultimate development) objective on the one hand, and their (immediate, short-term) outputs on the other hand. In varying degrees, these results reflect the (expected or planned) performance of the pertinent policies, programmes or projects.

C. The logical framework

At the planning and design stages, therefore, it is critically important to ensure a closer matching or correspondence between the desired outcomes and impact and, on the other hand, the set objectives and targets themselves. The logical framework (logframe) provides a feasible methodology and an analytical tool for matching purposes.[65]

The logframe is a 4-by-4 matrix. The programme and project elements are linked by or through the vertical columns to their respective components at different stages of implementation. This interlocking process, also known as the vertical (intervention) logic, is done clearly and in a structured and standardized manner.

However, these vertical columns do not provide adequate information and details for monitoring and evaluation purposes. For example, the ultimate (development) objective may be the existence of a culture of SME entrepreneurship, innovation and networking. The

[65] The logframe was first developed by USAID in the late 1960s and, in a number of variants, is now widely used by many agencies and institutions -- including the Asian Development Bank, the European Commission (DG VIII), DANIDA, GTZ, NORAD, Sida, ILO, UNIDO, UNDP and the World Bank. For further details, see Coleman (1987) and Commission of the European Communities (1993).

intermediate targets can be very wide-ranging. They may logically include the emergence of clusters and networks of highly competitive and innovative SMEs, and SME subcontractors in priority sectors and industries.

Table VII-1

The logical framework

Intervention logic	***Impact indicators***	***Verification information and sources***	***Risk and enabling factors***
Development objectives			
Intermediate objectives			
Results and outputs			
Activities			

The results observable from the above (top-down) sequence can be manifested as high levels of SME technological capabilities, productivity, output, export earnings, employment. Or they may appear in the form of denser networks of SME subcontracting linkages and more numerous SME clusters. Other indicators can be seen in higher amounts of credit and finance granted to a larger number of SMEs and SME start-ups, a larger pool of multi-skilled and technical workers etc.

The (multi-faceted) objectives in SME sector development and integration, as indicated in Chapter Two, are clearly ambitious, comprehensive in scope, heavy in resource requirements, and of a long-term nature time-wise. As such, the programmes and project activities and outputs to be delivered are very wide ranging in nature and number, and greatly intensive in depth and functionally interactive, too.

They may include a variety of SME capacity building activities -- on a self-reliant (toolkit-based) approach and, as necessary, supplemented selectively by BDS and extension activities on a cost-sharing basis. More funding resources and supplementary capital are also needed to underpin the establishment of ancillary infrastructure. And so are a conducive policy environment, a synergic partnership between the public and private sectors, plus external collaboration and partnering for SME development.

The horizontal rows (from the bottom up, matrix rows 2, 3 and 4 in particular) of the logframe serve to bridge the information gap. They specify at sufficient length the information and data needed as performance indicators and the sources for their verification.

The rows contain (a) the programme and project results to be expected at each corresponding level or stage of implementation; (b) a set of objectively verifiable indicators and measurements for that particular implementation level or stage; and (c) the corresponding inputs and means (or resources) and, on the other hand, the sources of information and data for quantification purposes.

Dependencies, such as the risk and enabling factors, can affect the implementation process and its impact, are specified in some detail right at the outset. These factors include unexpected and uncontrollable forces and influences (whether negative or positive). Or they can be anticipated and are expressed in the form of assumptions or pre-conditions. Risk factors and assumptions form an integral component for consideration in the logframe approach (see Box VII-3 below).

Box VII-3. Limitations of the Logframe Approach

Firstly, it is policy neutral -- in particular as regards such special considerations as gender, equity, participation of disadvantaged or marginalized groups, the environment etc. Secondly, it is only one of several available tools for performance monitoring and evaluation.

The logframe may, thirdly, give rise to rigidities in programme and project management, especially when higher-order results and external factors (the dependencies) are over-emphasized at the outset. On the other hand, the absence of incentives can induce trivialization of objectives and indicators.

As with most empirical approach, there are great difficulties in standardizing indicators and measurements for cross-comparison purposes. Impact indicators and measurements tend to be highly specific to the programme and project concerned. In fact, by the mid-1990s, the World Bank had published 18 volumes of supporting technical annexes relating to suitable indicators for various sectors and subsectors.

The above sectors include agriculture; economic adjustment; education; environment; financial sector; housing; industry and mining; oil and gas; population, health and nutrition; poverty reduction; power; private sector development; public sector management; technical assistance; telecommunications; transport; urban development; and water and waste water.

This "amazing" amount of materials emphasizes the customized nature of impact indicators and, on the other hand, the care and selectivity needed to ensure least-cost efforts in performance measurement. Mosse and Sontheimer (1996) contains a useful overview of performance indicators and related issues.

III. Performance evaluation

Indicators of programme and project impact and, more generally, information and data on performance measurement are useful for monitoring and tracking purposes. They reveal what has actually happened (*ex post*) with the implementation of programme and project activities and the associated delivery, in full or in part, of the related outputs, compared to what is expected to occur at the design stage (*ex ante*).

Generally, however, impact indicators are not sufficient in themselves to indicate *why* programme and project results are good or unsatisfactory. Nor do they explain why such results have turned out as they actually did. Performance evaluation is called for in this regard. But this assessment is not possible to undertake without the prerequisite information

and data on programme and project objectives, performance data and information, and a range of impact indicators.

Performance evaluation is an independent, systematic and objective assessment of the background, processes, and underlying factors relating to all three parameters of programme and project impact -- namely performance, relevance and sustainability. As such, the evaluation processes can be highly complex and time-consuming compared to, for example, the monitoring and tracking processes (see Box VII-4 below).

Box VII-4. A Bird's-eye View of the Performance Measurement Process

1. Definition of objectives

Policy, programme and project objectives and targets must be defined in concrete terms. They can also be specified as a measurable process in cases of intangible goals and concepts (such as enhancement, capacity building, cooperation etc.). The more succinct and precise these objectives and targets are expressed, the easier it is to devise indicators of impact and results.

2. Identification of risk and enabling factors

Programme and project activities are not totally insulated from global, regional and local developments. In varying degrees of seriousness, these exogenous influences and forces can affect, in a negative or positive manner, the results as well as the planned delivery of outputs from programmes and projects. Thus, the "dependencies" must be clearly stated and, if possible, some necessary defensive preparations be made or provided for at the on set of the design and implementation process.

3. Determination of measurement parameters and boundaries

First and foremost, performance indicators must be verifiable. Thus, conceptual or intangible objectives (such as quality, enhancement, cooperation, networking etc.) must be broken down into specific dimensions and parameters which can then be quantified with reasonable accuracy.

Performance parameters. A range of measurements can capture the major elements in the sequence of (immediate) outputs, and (intermediate) outcomes and effects: quantity, quality, target groups (and their compositions), scope and coverage, place and localities, time and period, and cost and logistics. These are largely primary impact indicators. Two other popular measurements of the lower-order or intermediate results of programme and project performance are known as effectiveness and efficiency coefficients or indicators.

Relevance and sustainability. These two impact parameters relate to higher-order (intermediate and long-term) results. As such, the specification of feasible and affordable indicators, and related verification sources and processes, are the difficult and time-consuming tasks in performance monitoring and management. For these reasons, the available indicators developed for practical purposes tend to stop short of measuring the relevance, and especially sustainability, of programme and project results.

4. Collection of performance information and data

Among the possible sources of information and data are official records of programme and project activities. The external records of such activities include surveys and interviews; contents of audio,

visual and written materials and communications from the target beneficiaries, peers and counterpart personnel etc.

Major considerations in any collection process are how hard, how long and how costly to obtain the needed information and data, and how reliable they are. In addition, whether it is possible to construct additional indicator from the collected information and data.

Source: Asasen, Asasen and Chuangcham (2000)

The evaluation of a programme and project can be undertaken as an internal or external exercise. But it has to be a time-bound activity, and is normally carried out on a selective basis because of practical necessity (to minimize delays or the scope for data collection etc.), and/or severe constraints on budgetary and other resources.

Substantively, a performance and impact evaluation can be carried out on the basis of (a) a programme or its elements; (b) a single project or a cluster of projects; (c) a process; or (d) a specific theme or a focus of policy. Selectively, programme elements or project activities of a strategic bearing or of great importance, in terms of their cross-cutting or cross-sectoral influence, can also be a subject for evaluation (more below).

The evaluation exercise can be conducted at mid-point of implementation to obtain indications of current problems and prospects for success (see Box VII-2 above). Terminal and *ex post* evaluation provides a more complete picture, and are therefore of wider application for the selection, design and implementation of future or follow-up programme and project activities.

As a whole, the core elements of performance evaluation include (a) a set of findings, (b) conclusions, (c) recommendations, and (d) lessons learned. Box VII-5 below contains a sequence of preparatory steps for the exercise.

Box VII-5. A Planning Framework for Performance Evaluation

In practice, a typical planning framework for programme and project evaluation may involve the following steps.

- *The construction and collection of baseline data relating to the issues and problems to be considered and addressed.*
- *Further clarification of programme and project objectives, and the setting up of specific goals and targets for assessment to be carried out.*
- *Establishing a consensus as regards performance and impact indicators among stakeholders.*
- *Identification of the sources of data and information, and agreeing on the processes of collection, generation, processing and usage.*
- *Specification of the reporting requirements and schedules (format, frequency, and distribution); and*
- *Drawing up the implementation and progress schedules, and assigning responsibilities for follow-up purposes.*

Generally, the timeframe and frequency for monitoring and evaluation depend on the nature of the programme and project activities concerned. UNDP practices are illustrative in these regards.[66] For indicative planning purposes, the budget is around US$ 35-40,000 for a for single-project evaluation, and US$ 50,000-100,000 for a cluster evaluation. Three weeks are the average length of the evaluators' field mission.

Evaluations carried out by members of the European Union and other European donors focus mainly on projects and, to a lesser extent, thematic areas. Such exercises are relatively limited in number -- clustering around 20-25 assessment studies, with a few in the range of 40-60 studies, a year. These account for around one to eight per cent of the total number of (ODA-based) projects funded by these donor countries (Sida and UNDP, 1997: 49-50; and UNDP, 1997: 55-56).

[66] For *multi-year projects*, there is an annual Tripartite (monitoring) Review, and the annual Project Performance Evaluation Report. Provisions are also made for mid-term, terminal (in-depth), and *ex post* project evaluations. For country programmes (CP), the annual and mid-term (3rd year) monitoring reviews tend to focus on the management of resources as tentatively provided for under the "indicative planning figures". The terminal CP report, normally undertaken near the 5th year, embodies a detailed impact evaluation.

Mandatory evaluation is to be carried out (a) for (large) programmes and projects with a budget of at least one million United States dollars; and (b) for technical cooperation support (to beneficiary institutions) of 10 years' duration or more. Non-mandatory evaluation is selectively implemented on the basis of certain considerations and parameters which are not fixed. Some of these are discussed in connection with the planning framework for programme and project evaluation in the text.

Chapter Eight

CONCLUDING SUGGESTIONS

Contents

- **Intra- and extra regional interaction**
- **Portfolio of selected project profiles**
- **Meetings between SMEWG and donors**
- **Extra resources for SME-related work**

It was a great challenge to prepare, as well as deep satisfaction to complete, this proposed policy blueprint for ASDD 2002-2012. This bulky policy blueprint embodies the firm conviction of many in the appealing and enduring values of entrepreneurial drive and private enterprise.

SMEs can be leveraged into competitive, inter-linked and innovative businesses –all in combination with judicious oversight from government and a propitious environment of external development and co-operation. What is needed now is a firm and sustained resolve for action among all stakeholders, both intra and extra regional.

The following suggestions are made in the above spirit. They are to assist in the operationalization of policy approaches, measures and options which are deemed suitable, feasible and hence selected for implementation at the regional, subregional and national levels as part of ASDD 2002-2012.

1. Intra- and extra regional interaction. It was pointed out in Chapter Six that complementarities can be seen in, and collaborative efforts are applicable to, virtually all the proposals in the policy blueprint and in the RAP as well (Tables VI-1 and VI-2). These complementary efforts range from an on-going dissemination of high-quality information, periodic exchanges of views and policy experiences, to joint research and capacity building activities.

In the context of information exchange, a cost effective modality can be considered. In its meetings, the ASEAN Working Group of SME Agencies (SMEWG) may wish to allocate a reasonable time (say, at least two hours) for the purpose of ensuring more frequent exchange of views and experiences on an intra-regional basis. Or the frequency of meetings can be optionally increased to accommodate some specific or special needs (more below).

The subject matters for exchange and interactions may be pre-selected (for example, at the previous SMEWG meeting) to facilitate advance preparations. In the ideal scenario, the agenda for such exchange and interactions can even be fixed one year in advance. The (rotating) host countries can take the lead role in arranging for the briefing or presentation to SMEWG; as necessary preferable on a non-official basis (and thus not reported) to encourage active participation and frank assessment.

A solid action programme in support of SME sector development and integration in ASEAN is likely to be of significant interest to ASEAN dialogue partners and organizations. Collaboration can be expected not only in terms of participation in meetings, including those convened by SMEWG, but also in financial and technical support for, and direct involvement in, project implementation itself.

2. Portfolio of Selected Project Profiles. The pilot projects and other policy measures suggested in the blueprint may be considered and selected for implementation by SMEWG**.** Table VI-2 (in Chapter Six above) can assist in the process by giving a brief overview of the approaches, focus and other characteristics of the pilot projects and policy suggestions.

Once the selections are made, brief project profiles can be drawn up. Most of the details as regards the pertinent context, background and justification are available form Chapters Two through Seven of the policy blueprint. They can be consulted and adapted, as appropriate, in compiling the project profiles.

The relevant Unit in the ASEAN Secretariat can be requested to prepare a collection of project profiles. Additional suggestions, made by SMEWG members during the project selection process, can be reflected or incorporated into the prepared profiles, as needed. Each profile can be 5 to 8 pages long.

3. (Extraordinary) Meetings between SMEWG and Donors. The portfolio of project profiles thus completed may be sent for the advance attention of all ASEAN dialogue partners and organizations, other donor countries and aid agencies. Many civil society organizations have a mandate or interest in supporting SME development in ASEAN. They can also be informed and invited for the same purpose.

Special meeting(s) can then be convened by SMEWG with all those interested in collaborating with ASEAN in fostering SME development and linkages; parallel session(s) can be held with non-governmental organizations, as necessary. Collaboration can be in terms of technical and financial support, in participation as a project beneficiary or facilitator, and/or in the project implementation process itself.

Project profiles, as endorsed or funded in principle in the meeting(s), can then be enlarged (with suitable incorporation of views or materials as suggested by donors and others) into full-scale project proposals for internal endorsement. Again, the relevant Unit in the ASEAN Secretariat can be requested to prepare all these proposals and get them cleared for submission for external funding.

4. Extra Resources for SME-related Work. Many of the proposed projects and focal areas for policy attention are quite demanding in scope. This applies regardless of whether they are in SME capacity building, or in carrying out periodic surveys for SME assessment and benchmarking, or in conducting policy-based research activities.

Many activities and proposals will also require on-going implementation in the longer term or during the ASDD 2002-2012. The number of SME beneficiaries so involved can thus easily be in the hundred thousands within the region.

All these considerations call for additional resources for SME-related responsibilities at the national level. But almost all of the suggested activities have strong elements of regionality. The wide ranging facilitation, co-operation, and integration measures are not limited just to the promotion and deepening of intra- and extra-regional linkages in SME capacity building, SME evaluation and benchmarking, SME complementarities and linkages in production and marketing and so on.

As such, the additional provision of a large number of technical inputs in support of SME development is essential at the regional level. And so are the needs for effective and timely backstopping and monitoring of region-wide activities, including through database establishment and information dissemination. Thus, more resources are also required at the ASEAN Secretariat to underpin SME-related responsibilities which will be significantly enlarged under the ASDD 2002-2012.

In sum, one of the most powerful and visible testimonies to political commitment and international co-operation in support of SME development is the successful implementation within ASEAN of a number of suggested policy measures in the short to medium terms (up to around five years). The SME sector surely deserves that much, being as it is the cornerstone of socio-economic growth with equity and stability in ASEAN and elsewhere, too.

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About the Authors

Choompon Asasen is Manager of the Human and Organizational Potential Development Center. He has had extensive experience as a researcher and project coordinator. His special research interests are on economic policy issues; recent assignments deal with intellectual property, however. His special geographical focus is on ASEAN and the Greater Mekong Subregion.

Kanchana Asasen is a Research Associate in HOPDC. She has worked extensively as a researcher, trainer and project coordinator. Her special research interests are on economic and social policy issues, and her special geographical focus is on ASEAN and the Greater Mekong Subregion.

Nataya Chuangcham is Managing Director of Ariel Company Limited. She is a business researcher and management trainer with training activities conducted in association with the American Management Association International. She has had extensive research and training experience in management benchmarking, ISO 9000 and total quality management. Her geographical focus is on ASEAN and the Greater Mekong Subregion.