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Majidah Hassan
University of Wollongong, mh868@uow.edu.au

Grace McCarthy
University of Wollongong, gracemc@uow.edu.au

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Title:

Influential organisational capabilities for SMEs' export performance: An exploratory study

Authors:

Majidah Hassan (Sydney Business School, University of Wollongong, Australia, and Universiti Malaysia Terengganu) and Dr. Grace McCarthy (Sydney Business School, University of Wollongong, Australia)

Abstract

Organisational capabilities that influence the export performance of Small and Medium Enterprises (SMEs) have been identified and discussed in previous studies which mostly have used SMEs in developed countries as their research sample. Thus, the empirical evidence from developing countries is still lacking. This exploratory study employs a resource-based view (RBV) perspective to understand how a set of organisational capabilities can influence the export performance of SMEs in Malaysia (a developing country). Based on in-depth interviews with CEOs or top level managers from twenty-three SMEs in Malaysia, the study found that capabilities to develop business networking, innovation capabilities, and capabilities to meet export standards are crucial for Malaysian SMEs' export performance. Interestingly, the findings indicate that SMEs need to focus on developing their business networking in order to enhance both their innovation capabilities and their capabilities to meet export standards, which in turn leads to export performance improvement. This study provides some insights into SMEs' export performance enhancement, particularly in developing countries.

Introduction

SMEs have become an important element in the economic development of most countries. As more and more SMEs engage in international businesses, there is a growing interest in these research themes (Kuivalainen, Puumalainen, Sintonen and Kyläheiko, 2010). Within these themes, the sub-topic of export business is prominent (Lages, Silva and Styles, 2009). It is well accepted that competing in international markets requires SMEs to have specialized capabilities (Kuivalainen, Puumalainen, Sintonen and Kyläheiko, 2010, Knight and Kim, 2009). Although globalisation has removed barriers between domestic and international markets which allow wider access for SMEs to export their product effectively, yet SMEs still face challenges in terms of resources constraints (Aaby and Slater, 1989, Zou and Stan, 1998, Wheeler, Ibeh and Dimitratos, 2008). In order to organize their limited resources efficiently, SMEs need to have organisational capabilities, since resources are not productive on their own (Grant, 2008). This is consistent with the RBV paradigm which assumes that strategic resources (including capabilities) are needed in order to gain competitive advantages.

Despite the growing interest in the internationalization of SMEs, there has been little research focused on developing countries (Tesfom and Lutz, 2006). Previous literature tends to focus more on developed countries (Aaby and Slater, 1989, Wheeler, Ibeh and Dimitratos, 2008). Given the differences between the characteristics of SMEs in developed and developing countries, especially regarding the level of tangible resources (Ghauri, Lutz and Tesfom, 2003, Tesfom and Lutz, 2006), it can be argued that the organisational capabilities that significantly contribute to enhance SMEs' export performance are likely to be unique and specific for SMEs in developing countries to achieve export success. Thus, this study employs the RBV paradigm to investigate the main capabilities considered as important by the SMEs' founders, owners or top level management perspective. This study aims to draw on the real life experiences from

CEOs, or top level managers of SMEs on the export performance in the context of organisational capabilities.

Literature Review

Organisational capabilities and export performance

Through the RBV perspective, Barney (1991) emphasized that firms may gain competitive advantage by focusing on their internal resources, which include physical, human, and organisational resources (Lages, Silva and Styles, 2009). Even though not clearly coming from RBV perspective, previous literature on export performance studies discussed the importance of internal resources and capabilities of firms for export performance. In their review article, Aaby and Slater (1989) categorised export success factors according to several internal influences, one of which is firm competencies or capabilities. Consistently, Zou and Stan (1998) also discussed export determinants within the context of internal factors which also included firm capabilities in their review. Recently, more export performance studies have been conducted by employing the RBV perspective such as Chew, Yan and Cheah (2008), Etemad (2004), Kaleka (2002), Knight and Kim (2009), Lages, Silva and Styles (2009). Drawing on the RBV and using Portuguese exporters, Lages, Silva and Styles (2009) found a positive relationship between internal factors (product quality and product innovation) and export performance. Their results are highly consistent with the RBV paradigm, according to which, capabilities become a competitive advantage for the firm and lead to the enhancement of the SMEs' export performance.

SMEs' exporting in developing countries

Commonly SMEs have been described as flexible, entrepreneurial, research and design intensive firms, which offer some potential for SMEs to compete successfully in international markets (Etemad, 2004). However, the current environment in which SMEs are operating could cause barriers for SMEs to compete successfully in international

markets. Previously, researchers classified export barriers for all SMEs, regardless of any differences in their country context (Leonidou, 2004). In other words, they portrayed their findings as universal, even though the sample used in their research was mostly from developed countries. Hence, the findings from those earlier studies may not be directly applicable to SMEs in developing countries. An interesting literature review article prepared by Tesfom and Lutz (2006), that comprehensively reviewed 40 articles (1980-2004) over a period of twenty-five years which used SMEs in developing countries as their samples, suggested that the type of export barriers for SMEs in developed and developing countries are similar. They concluded that the differences are not related to the type of export barriers, but only to the environment in which the SME is operating.

Neupert, Baughn and Dao (2006) found that most of the barriers faced by Idaho firms (which represented developed countries) can be categorized as external (Neupert, Baughn and Dao, 2006). The problems were mostly due to differences in rules and regulations, and socio-cultural and procedural differences. It can be concluded that the challenges for firms in developed countries are more related to the process of exporting rather than problems that relate to the product itself. In contrast, within the same studies, firms from Vietnam (which represented developing countries) showed that their main problems were related to poor product quality or that the product did not reach to the standard of the specification that has been requested. It seems that the problem is fundamentally one of effective management skills which may require greater managerial capability of Vietnamese exporters.

Tesfom and Lutz (2006) agreed with Neupert et al. (2006) that exporters from developing countries need to concentrate on technical capability and knowledge standards to ensure that they can produce export standard products. In order to reveal a set of capabilities relevant for SMEs' export performance especially from developing countries, more research needs to be conducted directly in developing countries (Ghauri, Lutz and Tesfom, 2003). As showed in the Table 1 below, the findings from recent studies in developing countries seem consistent with what has been discussed by Neupert, Baughn and Dao (2006) and Tesfom and Lutz (2006). Thus, this study aims to explore in

more detail the main capabilities that can be considered important for SMEs in developing countries to enhance their export performance. In this study, the research samples are from Malaysian SMEs (a developing country).

Table 1: Recent studies on export performance of SMEs in developing countries

Authors	**Countries**	**Findings (Capabilities that positively relate to export enhancement)**
Altintas, Tuncer and Talha (2007)	▪ Turkey	▪ Capabilities to meet host countries' procedural requirements
Estrada and Heijs (2006)	▪ Mexico	▪ Capabilities to meet export standards ▪ Innovation capabilities
Koksal and Kettaneh (2011)	▪ Turkey ▪ Lebanon	▪ Capabilities to meet export standards (procedural) ▪ Innovation capabilities (packaging design and production capacity)
Nguyen, Pham, Nguyen, and Nguyen (2008)	▪ Vietnam	▪ Innovation capabilities
Okpara and Kumbiadis (2008)	▪ Nigeria	▪ Capabilities to develop networking (gathering information from others) ▪ Innovation Capabilities (develop new products and improving existing products)

Methodology

Qualitative research is used to develop an in-depth understanding of human behaviour. The approach focuses on the reasons underpinning various aspects of behaviour and attempts to develop comprehensive detailed explanations of an issue within the research (Saunders, Lewis and Thornhill, 2003). Therefore, in order to understand how organizational capabilities affect the export performance of Malaysian SMEs, this research employed the qualitative method in answering the research question.

The technique used is in-depth interviews (face-to-face interview) with SME owners or top level managers who have the potential to answer the interview questions accurately. A semi-structured interview guide was designed based on the literature on organisational capabilities and SMEs export performance. The main purpose of conducting in-depth interviews is to gain rich and detailed answers (Bryman and Bell, 2007). Carson et al. (2001) and Malholtra and Birks (2003) found that for business research, in-depth interviews (semi-structured or unstructured) are the best method to investigate an individual's behaviour and are effective in collecting data from CEOs, owners or top managers.

The rationale behind the selection of Chief Executive Officers (CEOs), owners or top level managers as interviewees is that these executives have the most comprehensive knowledge of their organization's characteristics, strategy, performance, and play a major role in decision-making (Otero-Neira, Martti Tapio and Fernandez, 2009). This advantage will compensate for a commonly identified limitation of choosing CEOs or owners as the interviewee (e.g. bias in providing information) (Otero-Neira, Lindman and Fernández, 2009). Furthermore, Spence and Crick (2006) stressed that the use of interviews with other members of the respective organization to avoid bias due to interviews with CEOs, owner or top level manager provides little useful information since they did not have the depth knowledge to answer the questions being asked.

In developing countries like Malaysia, it is easier to access business if there is a recommendation from government agencies (Thai and Chong, 2008). Therefore the list of recommended SMEs in the Food and Beverage industry from Malaysia External Trade Development Cooperation (MATRADE) has been used to identify the sample for this study. Twenty-three face-to-face interviews were undertaken with top level managers or CEOs who were involved directly in their firm export business.

Findings

The results of the interviews are presented in Table 2. As shown in Table 2, the study found that capabilities to develop business networking, innovation capabilities, and capabilities to meet export standards are important for SMEs' export success in Malaysia.

Table 2: Summary of interview results with CEOs or top level managers of 23 SMEs

Organisational Capabilities	**Sub-categories**
Capabilities to develop business networking	▪ Gathering feedback on current markets
	▪ Gathering information for business improvement
	▪ Developing cooperation for business improvement
Innovation capabilities	▪ Redesigning packaging to meet export standards
	▪ Conducting R&D for new product development/product improvement
	▪ Increasing production capacity
Capabilities to meet export standards	▪ Monitoring quality of product to meet export standards
	▪ Investing in export standards/certifications

Capabilities to Develop Business Networking

Capability to develop business networking refers to "a set of intangible assets that reflect a series of interactions occurring between the interrelated parties involved in the export venture relationship" (Lages, Silva and Styles, 2009 p. 51). External relationships can create opportunities to acquire information, solve problems, expand market shares, and ultimately helps add value and enhance strategic capability (Zehir, Acar and Tanriverdi, 2006). As one participant commented:

> *Yes, business networking has great influence on our export performance. This is the basic fact. You need to understand how things work before you go for export. Why some companies can export? Why some companies cannot export? This is because of their business networking.*

Gathering feedback from export customers Demonstrating the importance of following up with export customers, one of the participants mentioned that follow-up is necessary since the foreign distributors commonly understand their markets better than the exporting company. Follow-up is also important to show that the exporter is serious in doing business with those export customers and this can help them to sustain their business. As suggested by one of the participants:

> *"Let say we did our first transaction with one of our foreign agents, and then we did not follow up. That export customers will think that we did not have interest anymore to do business with them. Maybe we can only get one transaction from them but still we need to do the follow up, we need to ask them how about the next orders. We don't want to sell only one time. We want continuous sale, we want to sustain our business."*

Meeting export customers at their places to get current feedback was also highlighted as good practice in the interviews. Some participants mentioned that they will meet with their export customers face-to-face if necessary. For example, one of the participants commented:

"Yes, we only go there to meet our export customers if it's necessary. We will fly to overseas once in 2 to 3 months. As an example, I went to Dubai early of this year, then Manila, and the latest is Sydney. Next month, I will fly to Germany. From Germany, I will fly to Miami, and November I will go to Korea."

Gathering information from others for export improvement Most participants stated that the capability to develop good relationship with others enables them to gather information that can improve their export business performance. A total of twenty-two of the twenty-three participants agreed that a good relationship with government agencies enables them to gather information that can improve their export performance.

In Malaysia, the government agency Malaysia External Trade Development Corporation (MATRADE) plays a major role in helping Malaysian firms, including SMEs, in export. All participants were registered members of MATRADE. Most of them agreed that by becoming a member of MATRADE, they can maintain awareness with information about programs provided by the government to enhance their export business, such as opportunities to participate in international exhibitions organised by government agencies where a part of the participation costs is covered by the government. As suggested by a participant who explained:

"We registered as a member of MATRADE. So whatever information about exhibition, they will inform us and invite us to join. So, from the membership, we will get the opportunity to involve in exhibition, we can promote our products, and we can attend business meeting. From the business meeting we will get the opportunity to meet the potential customers. MATRADE will match our time with the buyers. Let say for the first day of exhibition, our schedule is to meet the potential customers from Australia, London, and Kenya. So even though we are not going to overseas, we still can get the opportunity to meet potential foreign customers."

Most participants believed that participating in government agency programs such as seminars, workshops, and other development programs, can enhance their knowledge of export business and motivate them to compete internationally. Recognising the

importance of gathering information by participating in government programs, one of the participants commented that exporting directly overseas without participating in government programs is like blind people trying to walk. In other words, participation in government development programs can provide companies with sufficient information about export business, which can reduce the export risk, especially when companies are still new to export business.

In addition to the ability to gather information from government for export improvement, some participants also highlighted that participation in programs provided by trade associations can provide similar benefits.

Developing cooperation with others for export improvement The findings from the interviews revealed that cooperation between SMEs and others was formed for a variety of purposes. The purposes highlighted in the interviews were: productivity improvement, new product development, product quality development, promotion, new export market penetration, packaging improvement, and new technology implementation.

Fourteen of the twenty-three participants emphasised the importance of developing cooperation with government agencies to improve their export performance. Most of the participants agreed that product improvement and new product development is important in order to stay competitive in export business. However, most of them lacked experts and laboratory facilities in which to conduct research and development. Hence, they cooperate with government agencies that have suitable laboratory facilities and experts to conduct research and development that can improve products or develop new products for them. As indicated by one of the participants:

> *"We need to compete globally so we need to have the ability to follow the global trend. We don't want to be left behind. So we need to know the new technology that relates to this industry. Yes, we are SME and we don't have the expert in our company but we can always collaborate with other agencies that have expertise in research area. This can help us to produce the products with the latest technology and at the same level with products from other countries."*

Beside government agencies, the participants also recognised the importance of creating cooperation with foreign distributors (export customers). This was emphasised by eleven participants during the interviews. The main purpose highlighted in interviews is to cooperate in product promotion. The participants mentioned that it is important to provide marketing support to their foreign distributors. Participant from Firm-08 explained that the importance of providing marketing support to foreign distributors is to demonstrate their willingness to help. The marketing support that they commonly provided was free gifts (such as t-shirts, mugs, towels, and bags), products brochures, banners, and also funds to cover some costs of promotion (ranging between 10% to 50%) conducted by foreign distributors in their markets.

The other purpose of cooperation between SMEs and foreign distributors that was mentioned by participants during interviews is to improve productivity by acquiring appropriate machines from their distributors. One of the participants indicated:

> *"Sometimes, if we don't have suitable equipments, the buyers will provide to us for their order. Such as steam cooker. We don't have steam cooker but the buyer want us to produce for them steam cooked prawns so they provide us the steam cooker. We have a good networking with them. The trust is there, because we are their regular supplier. So, we already developed the trust. That's why they provide us the steam cooker."*

Innovation Capabilities

The data shows three sub-categories under innovation capabilities: capability to conduct research and development (R&D) for new product development, product improvement, and quality control; capability to upgrade from semi-automatic machines to fully-automatic machines; and capability to redesign packaging to meet export standards.

Conducting research and development for new product development, product improvement, and quality control Most participants tended to use R&D for product

improvement, quality control, and new product development. All twenty-three participants mentioned that they used R&D for product improvement and quality control. Product improvement includes improving the nutrition of their products. R&D is also important for quality control in order to avoid defects in products. As an example, one participant mentioned:

> *"Even 0.005 defects, it will consider defect. There is no formula that saying, 'it's just 0.005 defects so it's fine'. Once defect it will consider total defect. That's why in food business, ongoing innovation is a must"*

In addition, nineteen out of twenty-three participants explained that they also used R&D for new product development. New product development involves creating a unique product. The other four participants mentioned that they are not really focused on new product development.

Some of the participants have their own R&D department with a laboratory and employees responsible for running the tests. However, some participants explained that they did not have their own laboratory due to financial constraints. Therefore they developed some collaboration with government agencies and used government expertise and laboratories to run their tests. As an example, one participant commented:

> *"We started our research with cooperation from MARDI Kota Bahru. Based on that research we managed to improve our quality of soy sauce and we also started to produce other sauces such as chilli, tomato, oyster, and black pepper."*

(MARDI is Malaysian Agricultural Research and Development Institute.)

Upgrading operational capacity The other capability under this category is changes from semi-automatic machines to fully-automatic machines. Semi-automatic machines for production need more manpower compared with fully-automatic machines. Sixteen participants commented that they had changed from semi-automatic machines to fully-automatic because fully-automatic is more suitable for export business which commonly

involves large production volumes. The other seven participants identified several reasons why they still used semi-automatic machines: financial constraints, their factory structure was not suitable for fully-auto machine due to the size and weight of the machine, and the percentage of their export sales was still low so that semi auto-machines were still adequate.

Redesigning product packaging to meet export standards Most participants commented that they needed to redesign their packaging in order to meet the export standards. Some of them needed to invest in buying new packaging machines in order to produce products that have export standards of packaging. Most of them changed their packaging based on export customers' requirements. For example, one respondent commented:

> *"Our packaging depends on the customers' requirement. Some of our customers ask us to change the packaging and we did because it is worth it to change. It is worth it because their order is big and on regular basis. We use different packaging for local and export markets. For local, we use can for packaging, and for export markets, we use box. The design is based on customers' requirements. Some of our customers are ok with our design so we don't have to change it."*

Capabilities to gain Export Standard/Certification

Investing on export standard/certification Most respondents tended to invest in export certifications or standards. The certifications that they managed or tried to get are Hazard Analysis Critical Control Point (HACCP), International Organization for Standardization (ISO), Good Manufacturing Practice (GMP), Halal Certification (The certification that tells Muslims that the ingredients and methods of production of products are according to Islamic law), and the certification from the Health Ministry of Malaysia. Most of them already have all the certifications. A few did not manage to get all the certifications because of various reasons: financial constraints and documentation or incomplete application paperwork. In relation to financial problems, one respondent stated:

"Yes, if you look at ISO, they need documentation. So actually we can do it, because it is just a matter of documentation. But why we can't make it? It involved many aspects and most important aspect is money. If we have enough capital we can buy the system, we can buy latest technology for our machine, and many more… We also can provide uniform to all of our staff. Even though we have our own plant, but there are many more aspects that we need to improve: factory layout, fire safety system, water system, the capacity of electricity. All those things that we still need to improve. That's why we still cannot get ISO."

However, most of the participants that faced financial problems in trying to achieve export standards have made an effort to get help from the government. For example, another participant mentioned:

"We need to invest a lot of money for HACCP. Then, we still don't know the risk of that investment. However, we are working toward HACCP standard. We and many other SMEs with the help of government, we are working toward HACCP standard."

Monitoring quality of product to meet export standard Most of the participants also agreed that their product quality needed to meet export standards. In addition, four participants stressed that even though they are SMEs manufacturers, their products needed to be at the same quality standard as large firms. Another three SMEs highlighted that they pay serious attention to product quality: from the quality of raw materials to the quality of the end products.

"I believe one of the important points to be a successful exporter is product itself. Our success starts from product. Everything starts from products. So your products must be in a good quality because if it is not, you cannot sell in international markets or even in local market."

In fact some participants did not believe in the importance of the uniqueness of the product in order to become a successful exporter. They believed product quality was m more important than product uniqueness. As one of the participants mentioned:

"For me I think it is quite difficult to find the product that really unique. I think generally the product is the same only the value added that has been made on the product is different. So product uniqueness is not really important but the product quality is important. If you want to export your products especially to developed country, you need to really care about your quality. You need to meet their standard. From the quality of your raw materials to the quality of your packaging. Sometimes, SMEs tend to care less about product quality. You cannot do that if you want to export."

Discussions

The results from this study reveal that SMEs in Malaysia need to have capabilities to develop business networking in order to enhance their performance in export business. The results also suggest that SMEs need to develop their relationship with government agencies, trade associations, and foreign distributors. This is in line with the findings from Ling-yee and Ogunmokun (2001) that the relationship between channel cooperation and export performance is positive and important. In Malaysia, government agencies provide export market information such as trade fairs, export workshop and seminars, and overseas training programmes (Mahajar and Mohd Yunus, 2006). Most of the participants in this study agreed that networking with government agencies will provide export market information and other assistance which is consistent with research by Ali and Shamsuddoha (2007) who found that government export assistance programmes play a significant role in the Bangladesh exporting firm's internationalisation process. The cooperation that SMEs develop with others can help them to enhance their innovation capabilities (e.g. through providing instruments and experts to conduct research and development) and their capabilities to meet export standards (e.g. provide financial grants to invest in meeting export standards).

Similarly the networks that respondents developed with trade association and foreign distributors provided them with information updates. Respondents believed that their

relationship with trade associations and distributors may influence their export performance. This is consistent with the findings from Wilkinson and Brouthers (2006) and Koksal (2008). In addition, Sousa and Bradley (2009) emphasised that cooperation between firms and distributors is important because it can lead to strategic gains and a positive effect on export performance.

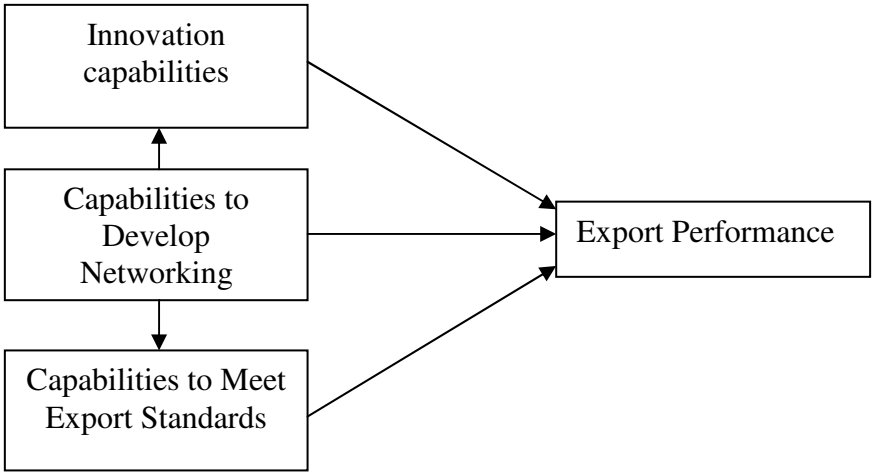
Innovation capabilities have been highlighted as important from this study (new product development and product improvement), but it is common for SMEs especially in developing countries to lack knowledge and research instruments. Hence, they cannot conduct R&D properly. However, through good networking with others (e.g. government), access to suitable help is available for SMEs. This finding is consistent with findings from studies conducted in other developing countries such as Vietnam, Nigeria and Mexico (Koksal and Kettaneh, 2011, Nguyen, Pham, Nguyen and Nguyen, 2008, Okpara and Kumbiadis, 2008)

The capability to increase production capacity also has been highlighted by the participants in this study as an important innovation capability. Most of the participants in this study mentioned that they changed semi-automatic machinery to fully-automatic machinery. They believed that to successfully deal in export business which normally involves larger volumes of production, they need to use fully-automatic machines. This is in line with Nguyen et al. (2008) who found that the ability of the firm to introduce new production processes or new technology (e.g. new machinery) has a significant relationship with export performance. In more recent studies in developing countries, Koksal and Kettaneh (2011) concluded that high performing exporters from Turkey and Lebanon tend to increase their production capacity in order to meet export demand.

This study also found that redesigning product packaging to meet export standards seems to be important for export success in Malaysia. This is consistent with research by Koksal and Kettaneh (2011) who emphasised that SME exporters that have high performance in their export business tend to have better product packaging compared with lower performing exporters.

Similar to the innovation capabilities, the finding from this study also emphasised that the capabilities to meet export standards are important for Malaysian SMEs' export performance. However, participants in this study faced some problems, e.g. financial problems that hindered them from meeting export standards. Arteaga-Ortiz and Fernández-Ortiz (2010) revealed that barriers related to export standards or certifications become a significant barrier to direct or indirect exporting SMEs in less exporting countries. Here, the importance of capabilities to develop networking stands out. Relying on good networking with others (e.g. government and trade associations), SMEs can get help to solve the problem. Based on the findings from this exploratory study, the research proposes the theoretical framework shown in Figure 1.

Figure 1: Proposed theoretical framework based on research findings



Conclusion

The challenges faced by SMEs exporters are becoming more important and increasingly crucial for policy makers and practitioners to understand. The statistics show high failure rates among SMEs in many countries (e.g. US, Australia, Brazil, France, and New Zealand) (Mason, 2009). This fact shows that it is highly important to assist SMEs in

sustaining their growth. Zehir et al (2006) suggest that in order to sustain the good performance of business, firm need to enhance their organisational capabilities.

However, the capabilities that suit SMEs exporters in developing countries have received scant interest from researchers hitherto, since most previous studies tend to focus more on developed countries (Aaby and Slater, 1989, Wheeler, Ibeh and Dimitratos, 2008, Zou and Stan, 1998). Tesfom and Lutz (2006) concluded in their review article that the element that make SMEs in developed countries different from developing countries is the 'environment' where the SMEs are operating. Therefore the findings from previous research are not necessarily applicable for environment in developing countries.

Thus this study tried to partly fill the gap by conducting the research in Malaysia. The findings from this study show consistent results with other studies that have been conducted in other developing countries (e.g. Vietnam, Turkey and Mexico). In line with previous research on export performance conducted in developing countries, this study reveals that capabilities to develop business networking, innovation capabilities, and capabilities to meet export standards are important for Malaysian SMEs' export performance. Therefore, the findings from this study support the previous studies in other developing countries such as Altintas, Tuncer and Talha (2007), Estrada and Heijs (2006) and Koksal and Kettaneh (2011). Furthermore, the findings will be expected to form the basis for guidelines to SMEs, particularly in developing countries, to improve their performance in export and at the same time to improve their countries' economic growth.

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