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Competitiveness strategies of small and medium enterprises in transitional economies

Charles Harvie
University of Wollongong, charvie@uow.edu.au

Cong Luyen Viet Le
University of Wollongong, viet@uow.edu.au

Elias Sanidas
University of Wollongong, elias_sanidas@uow.edu.au

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Abstract

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COMPETITIVENESS STRATEGIES OF SMALL AND MEDIUM ENTERPRISES IN TRANSTIONAL ECONOMIES

Dr. Charles HARVIE
Associate Professor, School of Economics
Director, Centre for Small Business and Regional Research (CSBRR)
Faculty of Commerce, University of Wollongong, Wollongong, NSW 2522, Australia
Email: charvie@uow.edu.au

Mr. LE Cong Luyen Viet
PhD Student, School of Economics, Faculty of Commerce
University of Wollongong, Wollongong, NSW 2522, Australia
Email: clvl970@uow.edu.au

Dr. Elias SANIDAS
Senior Lecturer, School of Economics, Faculty of Commerce
University of Wollongong, Wollongong, NSW 2522, Australia
Email: esanidas@uow.edu.au

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ABSTRACT

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Introduction

According to the OECD the globalisation of economic activity affects SMEs in two ways. It opens new opportunities for outward expansion and growth for some SMEs. For the other much larger group it poses new competitive challenges from abroad in terms of inward globalisation (OECD, 1997). Audretsch (2003) also points out that globalisation impacts on SMEs in two major ways. The first is the facilitation of trans-national activities of SMEs. These range from exports, foreign direct investment to participation in global value chains. The second is the changing role of SMEs in domestic economies where SMEs are the agents of change in the knowledge economy.

The emergence of private sector SMEs in transitional economies coincides with the process of globalization as a growing and irreversible trend in the world since the 1990s. There has been increased integration in the production process, the removal of barriers to trade and investment, and rapid technological advances (Hibbert, 2000). As such the participation of SMEs in transitional economies in the global economy could be an interesting issue to examine.

This paper focuses on the participation of SMEs in the global markets. In particular, it discusses the strategies that are relevant to SMEs in **transitional economies**. The paper argues that SMEs in general and SMEs in transitional economies face many distinctive barriers in international markets due to their smallness. However, the paper presents several competitive strategies that are relevant to SMEs in transitional economies to over come the barriers. They include subcontracting, participating in value chains, developing niche markets and networking. The paper demonstrates with the example of Vietnam that there is a long way to go for SMEs in a transitional economy to fully participate in the global market.

This paper is structured as follows. The next section discusses the barriers that SMEs in general have to face in the increasingly integrated global economy. The third section highlights competitive strategies that are relevant to SMEs in transitional economies. The fourth section presents a case study and examines the participation of Vietnamese SMEs in the global market through their export activities. The last section summarises the paper and offer some policy recommendations.

Barriers to Accessing International Markets

It is commonly believed that success in foreign markets requires large size and small firms were thought to be at a disadvantage over larger firms in foreign markets (Gomes-Casseres, 1997). Thus, Chandler (1990) declared that "to compete globally you have to be big." Indeed, small firms have to face distinctive barriers in international markets compared with those faced by large enterprises.

For most small firms high fixed costs constitute the most significant barrier in the internationalisation process. The costs of learning about foreign environments are quite large for small firms. These include the costs of doing market analysis abroad, purchasing legal consulting services, translation of documents, adaptation of products to foreign markets, travel expenses, not to mention a higher business and financial risk (European Commission, 2004). In addition, establishing and maintaining foreign distribution and marketing networks costs small enterprises a substantial amount, both in absolute cost and as a proportion of total costs (OECD and APEC, 2007:12).

Another barrier for small firms is accessing information about other markets. The lack of information, knowledge and experience in international markets represents a major challenge to small firms. A recent OECD and APEC report concluded that three out of the four most serious impediments to SMEs' access to international markets are about understanding overseas markets. Small firms have difficulty in identifying foreign business opportunities, limited information to locate and analyse markets and an inability to contact potential overseas customers (OECD and APEC, 2007:12).

The distance of foreign markets also makes it difficult for small firms to internationalise. Traditionally, small firms find it hard to communicate at long distances. Nevertheless, the advances in telecommunication technologies have reduced the importance of distance substantially. They also reduce the cost of transmitting information across geographic space. The microprocessor revolution has made it feasible for nearly everyone to participate in global communications (Audretsch, 2003). Although communicating at long distance is no longer an issue, managing complex relationships at a distance remains a considerable barrier to small firms (OECD and APEC, 2007:12). Thus, it was found that most SMEs tend to move initially into markets that are either geographically or psychologically close. For example, over 50 percent of Australian internationalised SMEs carry out activities in New Zealand and in Southeast Asia while most European SMEs first target adjacent countries in Europe (OECD, 1997:44)

SMEs also face a number of business environment barriers in their internationalisation endeavour. They have to deal with two or more sets of regulatory requirements on product standards. Intellectual property rights protection is another problem in foreign markets for small firms (OECD, 2005:74). They will find it costly to do so especially in countries with a weak enforcement mechanism. Globalised markets also mean fiercer competition for small firms with the presence of foreign firms. According to OECD (2005), many impediments to SME internationalisation may originate at the level of the national economy, institutions, and general infrastructure – related to issues of competition policy, legislative and regulatory frameworks, telecommunications infrastructure, research and education policy. This is added to by the fact that SMEs are weak in negotiating with national governments compared with large enterprises (Gomes-Casseres, 1997).

Obviously, barriers to accessing international markets are not the same for all SMEs. Indeed, the nature and extent of such barriers are different for SMEs in different countries. In addition, they vary depending on the product, the market and the level of management of the firms (OECD, 1997). Several of the above barriers actually overlap or come as the result of the lack of resources of SMEs. Evidence from an UNCTAD survey of small and medium-sized trans-national corporations in 1993 showed that internationalised SMEs tend to be larger, more capital rich, more productive and profitable (Buckley, 1997). Nevertheless, the nature and size of transaction costs affecting the internationalisation of SMEs can change. For example, the availability of new communication technology and emergence of e-commerce have provided small firms with lower costs of transacting with suppliers and customers (Hallberg, 2000). This has enabled many small firms to participate in wider markets and link with other firms.

SMEs in transitional economies have had limited experience in international trade. During the central planning period large enterprises were favoured over SMEs. There were restrictions to private SMEs and their international trading activities. Therefore, SMEs were not much exposed to foreign competition or exporting activities before making the transition to market economies. In addition, SMEs in transitional economies face higher transaction costs and have more limited access to credit and other inputs. As a result, they have greater difficulty penetrating export markets.

Table 1 summarizes the types of barriers as reviewed so far in relation to the four types of opportunity costs as suggested by Sanidas (2006). These costs correspond to four basic production processes that fully describe all activities and operations of firms as shown in this table. It becomes apparent from this table that SMEs face not only transaction costs but also knowledge costs (even more than transaction costs), kinetic costs, and strategic costs. Thus, for example "knowledge and experience in international markets" is a rather strong knowledge opportunity cost.

Table 1: Barriers as Opportunity Costs

Barriers	**Process of strategies (POS)**	**Process of wisdom (POW)**	**Process of Movements (POM)**	**Process of contracts (POC)**
	Strategic costs	**Knowledge costs**	**Kinetic costs**	**Transaction costs**
Learning re foreign environment		√√		
Doing market analysis abroad		√√		
Purchasing legal consulting services				√√
Translation of documents				√√
Adaptation of products to foreign markets		√√		
Travel expenses			√√	
Higher business and financial risk	√√			
Establishing foreign distribution and marketing networks			√√	
Accessing information re other markets		√√		
Lack of information		√√		
Knowledge and experience in international markets		√√		
Understanding overseas markets		√√		
Identifying foreign business opportunities	√√			
Inability to contact potential overseas customers		√√		
Distance of foreign markets			√√	
Transmitting information across geographic space			√√	
Regulatory requirements on product standards				√√
Intellectual property rights protection				√√
National competition policies			√√	
Legislative and regulatory frameworks				√√
Telecommunications infrastructure			√√	
Research and education policies		√√		
Entrepreneurship abilities	√√			
Managerial abilities	√√			

Despite facing barriers to entry in foreign markets, globalisation has created opportunities for the participation of small enterprises in international business. The next section discusses major strategies that SMEs in transitional economies can adopt to remain competitive in the global economy.

Competitiveness Strategies for SMEs in Transitional Economies

The OECD identified six principal competitiveness strategies of SMEs. They include innovation strategy, information technology strategy, niche strategy, network strategy, cluster strategy, and foreign direct investment strategy (OECD, 2000b). A more recent survey of SMEs in 19 European countries found that SMEs try to optimise their competitiveness by exploiting new business opportunities in the value chain, encompassing trade, cross-border clustering, cross-border collaboration, alliances or subsidiaries, branches and joint ventures abroad (European Commission, 2004). However, the above studies focussed on developed countries. The discussions below focus on strategies that are relevant to SMEs in transitional economies.

Subcontracting

Traditionally, it is expected that a small start-up firm slowly grows to become a large firm and expands further to participate in global markets. However, a 'symbiotic' relationship between small and large firms in the creative destruction process in the modern global economy is emerging. Small firms can now make intermediated expansion via larger multinational firms. This happens as global competition induces multinationals to source from the most efficient suppliers worldwide (Acs, Morck, Shaver, and Yeung, 1997:14). International production in the period of globalisation has led to the development of cross-border production operations, including partnerships of different types (OECD, 2000a:6). One type of networking is subcontracting relationships that facilitate economic specialisation of firms as well as superior access to information (OECD, 2000b:16).

Networks of mainly small firms, collaborating through specialisation and subcontracting, have been the key to the success of many industrial districts in developed countries including Italy (UNCTAD, 2005:146). The industrial district model consists of a more horizontally related network of firms. Meanwhile, Japanese firms rely more upon subcontracting and less upon vertical integration than firms in the West for the supply of parts and intermediate products (You, 1995:449). The long-term supply relationship between many parts makers or firms with specialised processes and large assembly makers, especially in the auto and electronics industries in Japan, has formed a social division of labour in the industrial production system (*shitauke*). This unique system for Japanese industry has been quite successfully transferred to other East Asian countries such as Korea, Hong Kong and Taiwan (Yoshio Sato, 1983). In fact, Korea has pursued a vigorous policy of mandating and encouraging subcontracting of SMEs by larger corporations and this has contributed to a change in industrial structure (OECD, 2000a:18).

Subcontracting is somewhat similar to the putting-out system which is a vertical inter-firm network frequently formed by large firms on the ordering side with SMEs as suppliers. In the putting-out system the large firms on the ordering side are usually wholesalers or commercial capitalists. They do not engage directly in the production process and only control SMEs as suppliers from outside the production process (Yuri Sato, 2000). In this system wholesalers assist, cooperate and provide benefits to SMEs through several mechanisms such as supplying raw materials, lending funds, and supplementing important facilities and tools. Unlike the putting-out system, the large ordering firm in subcontracting is often an industrial firm that engages in manufacturing activities as its main business. Therefore, subcontracting is based on technological necessity in the production process. SMEs are also more connected to their ordering firms in a subcontracting system than in the putting-out system (Adam, 2006).

In recent decades, the involvement of foreign subcontractors in developing countries has been increasing. Thus, UNCTAD (2005:122) gives the definition of subcontracting as a local firm manufactures a component or sub-assembly for a foreign manufacturer located either in the newly industrializing country or overseas. UNCTAD has shown that trans-national corporations (TNCs) and their affiliates have developed integrated business-to business strategies, providing suppliers and subcontractors with various modes of technical, human and financial support (UNCTAD, 2001).

Subcontracting is observed to be more prevalent in Asia than in Africa and Latin America. This may be due to the smaller markets as well as to the propensity of large firms to import a large share of their needed inputs from Asia (Liedholm, 2002). Business climate or environment, including the availability of suppliers of quality materials and government bureaucracy and regulatory mindset, are the issues affecting TNCs' decision to form subcontracting relationship with local small firms. Thus, TNCs were more interested in doing business in certain South-East Asian countries because of political stability, availability of competent suppliers and subcontractors and a fast growing domestic market but not in other economies in the same region with a volatile political climate (UNCTAD, 2005:46).

Evidence from surveys conducted in some Eastern European transitional economies indicate that these countries have been able to attract sub-contract work in the clothing industry from Western multinational companies based on their relatively low labour costs (Smallbone, Piasecki, Venesaar, Todorov, and Labrianidis, 1999). Thus, the sub-contracted work is in the more labour-intensive parts of the production of low or medium-quality products (Smallbone, Piasecki, Venesaar, Todorov, and Labrianidis, 1999:372). In transitional economies with small domestic markets and low purchasing power, such as the Baltic states, firms experienced the push factor to develop foreign markets (Smallbone, Piasecki, Venesaar, Todorov, and Labrianidis, 1999). In such a situation, subcontracting and other forms of collaborative arrangement with foreign firms offer certain advantages compared with other strategies, since they can reduce market entry costs and barriers, with lower associated business risks (OECD, 2000a).

Both transition economies in Asia, namely China and Vietnam, have been quite successful in attracting foreign TNC to subcontract their production. The relatively cheap and hard working labour and their geographic location the dynamic region in Asia, has made them a favourite destination for many investors. China has emerged as the largest recipient of FDI among developing countries, and in recent years and among the world's top recipient of FDI (UNCTAD, 2007). Meanwhile, Vietnam has also achieved remarkable success with FDI. Recently, it has emerged as the third largest recipient of FDI in ASEAN behind Singapore and Malaysia, surpassing the Philippines and Indonesia. This was achieved within a short period of time since the introduction of the foreign investment law in 1987 (Hafiz and Giroud, 2004). SMEs in China and Vietnam are involved in a variety of subcontracting activities ranging from hi-tech industries such as electronic and IT to labour intensive industries including garment, textile and footwear. A survey in 2002 revealed that 14 percent of SMEs had formal subcontracting relationships. Among them modern firms such as limited liability company had a much higher share reaching 28 percent (Kokko and Sjöholm, 2005).

Participating in Value Chains

Small firms can participate in the global market by becoming part of the networks formed by global suppliers and customers. This type of network is called a value chain. According to

Kaplinksy and Readman (2001:28) a value chain describes the full range of activities which are required to bring a product or service from conception, through the different phases of production (involving a combination of physical transformation and the input of various producer services), delivery to final consumers, and final disposal after use. SMEs may complement large firms in the value chains, exploiting advantages of flexibility and lower transaction costs due to close contact with customers and quicker decision-making, while large enterprises exploit different advantages of scale. Thus, TNC-SME linkages and global value chains could serve as a bridgehead to export competitiveness. This will happen with the right mix of small and large firms and an adequate division of labour that combines economies of scale with flexibility and the advantages of specialisation (UNCTAD, 2006:13-14).

In some global value chains, firms, and even clusters of firms, may undertake only a limited range of functions. Like subcontracting firms, they may work to designs provided for them, using materials which are sourced by other firms. But in this case, the "other firms" might be located thousands of miles away (Humphrey, 2003). Value chain cooperation also exists among SMEs. This appears to be much easier when it involves vertical value chain links than when it requires cooperation between firms doing similar things. For example, shoe, leather and machinery firms cooperate much more readily than do shoe manufacturers alone (Kaplinksy and Readman, 2001:41).

In addition to participating in value chains, it is important for SMEs to upgrade from low to higher value added activities in the value chains. The businesses suffering the most from new market conditions are generally those involved in activities at the bottom of the value chain, while enterprises involved in the finalisation of products have much higher chances of succeeding (UNCTAD, 2005:iv). Upgrading within global value chains depends upon firm level and cluster level investment in upgrading. There are two reasons for this. Firstly, there are areas where customers cannot, or will not, provide assistance. Secondly, if firms in the cluster can contribute their own upgrading efforts to the chain, this increases the value to the other firms in the chain and provides additional protection from substitution. Therefore, firm level innovation efforts are essential here (Lee and Chen (2000) as cited in Humphrey, 2003:20).

Vietnamese textile and garment industry has rapidly participated in the global value chain. Vietnamese firms supllied a wide range of global buyers from leading brand names to small regional traders. In this context foreign traders and garment producers play a leading role in connecting Vietnamese to global retailers. However, there are differentiated impacts with large firms such as SOEs have better access to the higher value chains while smaller private firms are restricted to small regional traders and less valuable markets (Nadvi, Thoburn et al., 2004).

Developing a Niche Market

An important strategy for SMEs is to develop niche markets. In this strategy SMEs choose to become sophisticated players in a narrow product line (OECD, 2000b:10). By pursuing this strategy, small firms not only could compete with larger firm but they could also reach to export markets (Harvie and Lee, 2005a: 18). Within industries, the mobility barriers are argued to allow small firms to find and defend strategic niches (Porter, 1980). Indeed, small businesses are found to be able to reduce or reverse the profit advantage of larger rivals in industries with heterogeneous activity mix (Bradburd and Ross, 1989). A niche strategy for small firms can be classified into two types. One is the specialised markets and the other is innovative niches (OECD, 2000b).

A traditional explanation for the success of small firms was that they make strategic choice. They focus on areas where there are no economies of scale or even some diseconomies of scale (Gomes-Casseres, 1997). In industries with product differentiation, the survival and growth of small firms depend on their ability to carve out their market niche and avoid head-on competition with large firms. Small firms may have the advantage in serving markets for specialised products and services whereas large firms tend to be strong in standardised markets (You, 1995:453). The flexibility of small firms enables them to become specialised in the market segments in which they have an advantage. Services, for example, tend to be specialised and dedicated compared to manufactured goods. Thus, there is a prevalence of small firms in the service sector (You, 1995).

SMEs in transitional economies can develop niche market strategies based on their comparative advantage. They can focus on specialised products for export or offer goods and services for domestic markets due to rising purchasing power in their economies and with their understanding of local markets. SMEs in developing economies in general and transitional economies in particular will find it more difficult to follow the 'deep niche' strategy which focuses on high product quality. According to Fujita (1995), in order to do this firms need to have proprietary technology, flexible management, organisational and market ability, quality control, after sales service, reputation and prestige and customer and supplier relations.

By pursuing a niche market strategy, many small firms are, in fact, large players in their niche. They occupy dominant market positions and outflank their rivals in terms of resources and capabilities. These firms typically rely on their own capabilities to exploit market niches (Gomes-Casseres, 1997:34).

Survey results show that Vietnamese SMEs' exports largely fall within the broad areas of the country's comparative advantages with labour intensive products have a larger share in SMEs' exports in the food and other manufacturing categories compared with that in Vietnam's total exports. The focus among SMEs is on rice crackers, furniture, garments, and handicrafts (Kokko and Sjöholm, 2005). These are currently the niche products for Vietnamese SMEs in the export markets.

Networking

Networking is formal and informal links between enterprises. It facilitates both increased economic specialisation external to the firm as well as superior access to information (Audretsch and Thurik, 2001:297). In the age of globalisation, inter-firm networks can help small firms to compete on a par with larger companies (Harvie and Lee, 2005b:18). Networks can allow accelerated and peer-based learning. They can facilitate the reconfiguration of relationships with suppliers to enable firms to innovate, and offer scope for increased efficiency through collective action (OECD, 2000c:28). Thus, the network structure allows firms to reduce costs and spur innovation by co-operating with or subcontracting to external firms (OECD, 2000b:17).

Networks can be formed on the basis of ethnic groups, industry, and societal organisations. It was found that community connections play a crucial role in the membership of African business networks (Biggs and Shah, 2006). Sharing cultural backgrounds, beliefs, and attitudes make it easier for members of the same ethnic groups to predict and understand the behaviour and needs of other members (Adam, 2006). Meanwhile, a network of firms in the same industry will help them to achieve collective action in the purchase of inputs or labour sharing (OECD, 2000c). Societal-based networks provide another avenue for firms to seek partners. They include the trade and industry associations and the voluntary agency federations who provide the benefits that could not otherwise be achieved by individual small firms (Adam, 2006).

When there is economic instability, market imperfections and weak legal institutions, inter-firm networks and relationships provide the mechanism for small firms to overcome institutional barriers (McMillan and Woodruff, 1999, 2002). As such networks are particular relevant to economies in transition. Empirical evidence from different country contexts shows that ongoing relationships among firms substituted for the missing institutions in the transition period (McMillan and Woodruff, 2002). Faced with difficult access to finance small firms in transitional economies also rely on partners in a business network. A survey of private firms in Vietnam revealed that firms provide more trade credit to customers indentified through business networks (McMillan and Woodruff, 1999). Personal network relationships such as the *guanxi* network in Chinese communities have been in existence for a very long time in the East Asian economies at different levels of development (Fulop and Richards, 2002). *Guanxi* is a key aspect of Chinese business aspects which is associated with doing business on the basis of personal relationships, building networks and strengthening business relationship (Freeman and Lim, 2008). In addition, the large Chinese diaspora has helped Chinese SMEs to expand their businesses to foreign markets (Hall, 2007). Similarly, there is a large Vietnamese disaspora in different countries including Australia, Canada, France and US. There are also business networks in Estern Europe and the former Soviet Union established by the students, guest workers and sailors in the earlier period (Beresford, 2008). New networks are being developed both domestically and internationally as Vietnamese businesses are expanding their activities.

The collaboration by small firms in networks as well as clusters could facilitate the joint assessment of market opportunities, enable participation in trade fairs, establish contacts with producers or buyers, facilitate the upgrading of technology, develop new products, restructure organisational production and capabilities, and improve product standards and the attainment of ISO accreditation to overcome the threats in the current globalisation of markets (Harvie and Lee, 2008).

Out of all these four strategies which ones are most suitable to assisting in lessening the impact of barriers to accessing international markets? The answer to this question can be best reached by examining the opportunity costs of Table 1 in relation to the characteristics of these four strategies. A more comprehensive study of these characteristics would allow us to complete our research. Until such study is carried out, the following Table 2 shows some *suggested* characteristics and their relationship with the findings of Table 1. From our suggested traits, it seems that networking is the best strategy to follow as it lowers all opportunity costs. However, we should bear in mind that all these suggested strategies are overlapping and interrelated to some extent. Surveys would more appropriately determine the relevant issues and tell us more concretely as to what are the advantages of each strategy regarding the lowering of the four types of opportunity costs. It is important to note that for transitional economies, wisdom (or knowledge) costs can be very high and common (as seen in Table 1) and hence a suggested strategy should at least address the wisdom costs as much as possible.

Table 2: Suggested Strategies and Their Pertinence in Lowering Opportunity Costs

	Strategic costs	Wisdom costs	Kinetic costs	Transaction costs
Subcontracting		√√	√√	√√
Participating in value chains		√√	√√	√√
Niche markets	√√	√√		
Networking	√√	√√	√√	√√

Export Strategies and Vietnamese SMEs

Essentially SMEs can be involved in exporting activities through two modes: indirect exporting and direct exporting. Many SMEs are involved in world markets as indirect exporters by supplying intermediate inputs or subcontracting to large firms (Biggs, 2002:8-9). Becoming indirect exporters could be a sensible choice for SMEs to bring their products to overseas markets. They can link up with TNCs or large domestic exporting firms and thereby integrate into global chains of production. The fast and efficient subcontracting SMEs provide critical flexibility and 'just-in-time' benefits to the supply chain which are an important source of competitive advantage in international markets (Porter, 1990 as cited by Biggs, 2002:9). Nevertheless, it is not impossible for SMEs to become direct exporters. As discussed above, SMEs can create competitive niches and prosper in world markets by working through industry-based clusters. Most industry clusters developing countries are based on family social networks which reduce the substantial transaction costs (Biggs, 2002:9). There are success export stories in developing countries in labour intensive sectors such as ceramics, garments, leather and shoes (UNCTAD, 2005).

Like their counterparts in other transitional economies, domestic Vietnamese firms do not have much experience dealing with international markets due to restrictions under central planning. Although businesses in the South had some experience in international trade before the ward ended, they suffered from the restrictions after the war ended in 1975. Even after *Đổi Mới* economic reform in 1986 there was a sceptical view about domestic private enterprises at least in the first decade after the reform (Ari Kokko and Sjoholm, 2000). Before 1998 most private and foreign enterprises were not able to obtain export quotas directly. It was not until December 1998 that export quotas were auctioned to state, private and foreign enterprises in an attempt to give export quotas to the best performing enterprises (Cuong M. Nguyen and Quan V. Le, 2005).

It was observed that Vietnamese domestic firms are only just beginning to emerge as significant exporters, following the relaxation of policies that had restricted opportunities for private firms to be directly involved in export activities (Mallon, 2007). Compared to other countries in the region, Vietnamese businesses are weak in many commercial skills, ranging from marketing capacity to having little business networks. For example, Vietnamese managers are still developing an understanding of the relationship between product quality and customer satisfaction in the international market (Neupert, Baughn, and Dao, 2006). In addition, Vietnam's competitors have invested large sunk costs to build up their capacity with a longer involvement in international trading. It will take time for Vietnamese SMEs to develop skills and build up networks with their overseas trading partners.

At the moment very few Vietnamese SMEs participate in direct exporting. A survey of 1,400 non-state domestic manufacturing SMEs with less than 100 workers in 2002 found that only about 3 percent of the surveyed firms participated in direct export activities. This is despite the fact that Vietnam had the highest export growth in the world in the 1990s (Ari Kokko and Sjöholm, 2005). It was concluded that the vast majority of small manufacturing firms in Vietnam are producing for the rapidly expanding domestic market (Ari Kokko and Sjöholm, 2005:162). Kokko and Sjöholm (2005:163) estimated that at most 16 percent of SMEs in the survey sample of 1,400 manufacturing SMEs have direct or indirect relations with export markets. This figure included firms that recorded either direct exports or formal subcontracting contracts or both of the two activities.

Table 3: Exports as % of SMEs Total Output and % of SMEs Engaged in Export

	Total sampe	Urban	Rural	Household	Private	Partnership and collective	Limited liability and shareholding
Exports as a share of output	16	22	5	14	4	16	20
Share of SMEs with exports	3	4	1	1	1	4	15

Source: Kokko and Sjöholm (2005)

Table 3 shows that urban enterprises are more export oriented than their rural conterparts. In addition, the more modern types of enterprise have higher export ratio. They include limited liability, shareholding and partnership companies. In addition, it was concluded from survey of SMEs in 2002 that exporting SMEs tend to have more workers than non-exporters (Kokko and Sjöholm, 2005). In fact, Kokko and Sjöholm (2005) found that firms in large urban centres (Ha Noi and Ho Chi Minh City) that had more than 100 employees, and that had been established as limited liability or shareholding companies, were more likely to be involved in exporting. Regression results with 1,150 Vietnamese firms in the manufacturing sector surveyed in 2005 also indicated that firm size, firm age and foreign ownership are positively related to the export probability of firms (Nguyen Hiep and Ohta, 2008). In a recent study about innovation and exporting of Vietnamese SMEs, it was found that product innovation, process innovation and modification of existing products are important determinants of exporting (Ngoc Anh Nguyen, Quang Ngoc Pham, Dinh Chuc Nguyen, and Duc Nhat Nguyen, 2007).

A closer look at the profile of exporting SMEs in the 2002 survey revealed that export producing SMEs have higher labour productivity (in terms of value-added per employee) than non-exporters. However, this is largely accounted for by the high productivity of the limited liability and shareholding firms that export in the sample (Ari Kokko and Sjöholm, 2005). Meanwhile, total factor productivity was found to have no statistically significant effect on the probability of firms exporting in a firm-level data analysis (Nguyen Hiep and Ohta, 2008). Exporting firms rely on comparative advantage (cheap labour and raw materials) (Ari Kokko and Sjöholm, 2005). As a result, firms that are more likely to be exporters in Vietnam are producing labour-intensive products or using labour-intensive technology (Nguyen Hiep and Ohta, 2008). They include firms producing garments, textiles, leather products, foods and beverages, non-metallic products, and wood and wood products (Ari Kokko and Sjöholm, 2005; Nguyen Hiep and Ohta, 2008).

The limited participation of Vietnamese SMEs in international markets is a concern for Vietnam's policy makers. Survey results in 2002 showed that SMEs were ignorant of trade liberalisation and economic globalisation. Over two thirds of SMEs do not know what further liberalization would mean to them and 82 percent of the surveyed SMEs did not take steps to cope with globalisation (Ari Kokko and Sjöholm, 2005). Nevertheless, the SME Development Plan for 2006-2010 set the target of doubling exporting SMEs to 6 percent by 2010. This ambitious goal is projected based on the expectation that the business environment, access to land, finance and skilled labour together with the improved competitiveness of the SMEs will be improved (MPI, 2006:76).

Conclusion and Policy Recommendations

SMEs are subject to many obstacles in the conduct of their business, which hinder their growth, development and participation in domestic and global markets. Most of these difficulties are related to access to finance, lack of skills, knowledge, information and technology as well as ongoing non tariff barriers facing SMEs in international trade. These go some to explaining the relatively poor contribution of SMEs in international trade, which is considerably less that that to domestic output and employment, despite many opportunities arising from the process of globalization and associated market liberalization. In developed, and indeed developing countries, SMEs have responded to the opportunities as well as threats from globalization by focusing upon innovation and knowledge, information technology, niche markets, networking and clustering and foreign direct investment as key strategies for competitive advantage.

As this paper has demonstrated the above difficulties are further compounded, or are more intense, in transition economies, where SMEs additionally face: a lack of market structures, institutions, and knowledge of conducting business in a market oriented economy; a lack of entrepreneurial skills; lack of finance; outdated technology; bureaucratic regulations and corruption; and less than supportive government officials and agencies. SMEs in Vietnam and China will inevitably face intense competition in the future, and consequently there is a need to tackle these difficulties as a matter of urgency. Competitiveness strategies based upon: subcontracting, participation in value adding supply chains, niche market development, and network participation and development appear to be the most appropriate way forward.

Finally, the role of government will be of crucial importance in the transition economies. Government will be required to put in place the necessary market oriented structures and institutions that will facilitate the establishment, nurturing and growth of SMEs. Bureaucratic regulations and corruption need to be tackled as a matter of urgency. Government and its agencies will be increasingly required to play a facilitatory rather than production role within the economy, one that embraces the market, private ownership and entrepreneurialism. Increased participation of SMEs in the global economy will also be essential and in this regard policy should aim at: encouraging the upgrading of skills and technology; providing information on market opportunities; facilitating access to small business finance; facilitating networking amongst SMEs and, where appropriate with large domestically owned enterprises as well as TNCs. The obstacles facing SMEs in the transition economies are immense, but the process of globalization will require their improved competitiveness and product quality if they are to survive let alone fully participate and benefit from it.

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