

Section II



CHARTING THE WAY FOR SME DEVELOPMENT

Chapter 3: Strategies for SME Development

Strategies for SME Development

CHAPTER 3

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Constituting more than 99% of total business establishments in Malaysia, it is clear that promoting a viable SME sector is essential in the nation's stride towards broadening the sources of growth and sustaining the growth momentum.

SMEs stimulate private ownership and entrepreneurial skills; provide broad based sources of growth whilst also acting as incubators for developing domestic enterprises into large corporations. However, SME contribution to the economy is still relatively small. In recognition of this, the Government has made the development of SMEs a high priority area. This is reflected in the national development agendas, namely the Ninth Malaysia Plan (9MP) and the Third Industrial Master Plan (IMP3), in which the key strategies for SME development is outlined for the 2006-2010 and 2006-2015 periods respectively.

SME Contribution to the Economy



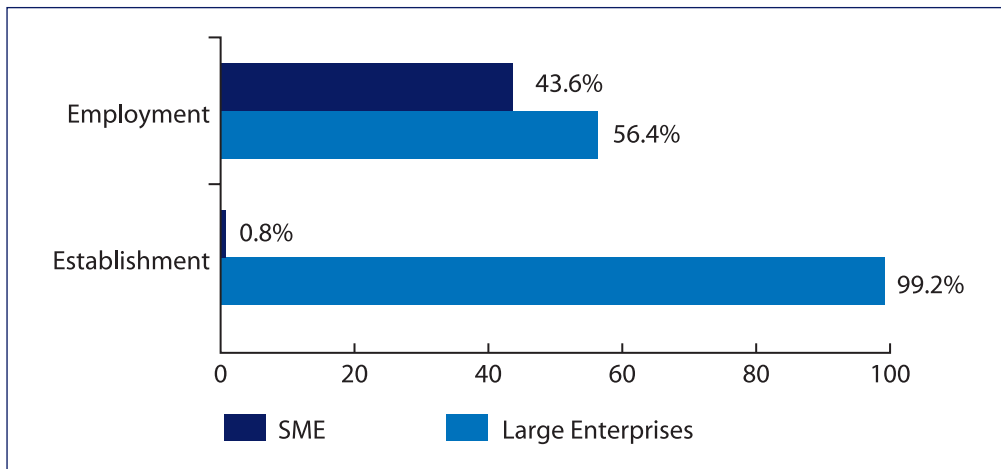
The 2005 Census of Establishment and Enterprise (Census) found that the bulk of business establishments (99.2%) is SMEs, of which about 80% are micro enterprises. The Census results also show that SMEs are a major source of employment, providing jobs for over 5.6 million workers and accounting for 56% of total employment. However SME contribution to the economy is still disproportionately low - SMEs contributed only 32% of gross domestic product and 19% of the total export value.

Macro Performance of SMEs	2003 (%)	2005* (%)
SMEs' contribution to GDP	31.9	32.0
SMEs' contribution to employment (excl. Govt.)	55.8	56.4
SMEs' share of total exports	18.9	19.0

*2005 data estimated based on the Census 2005's profiles and other relevant data.

Similarly, productivity levels in the SMEs were found to be significantly lower than large enterprises as they generated an average value added per employee of just RM14,740, far lower than the RM47,830 generated by large enterprises.

SME Contribution to the Economy



Sources: Bank Negara Malaysia

By prioritising SME development, the Government aims to increase SME contribution to GDP from 32% to 37% and total exports to rise from 19% to 22% by 2010.

1. The Ninth Malaysia Plan (9MP)

During the 9MP, the principal SME policy is the development of a competitive, innovative and technologically strong SME sector that is able to contribute to the domestic economy and compete globally. Strategies will be directed at acquiring technologies to propel SMEs up the value chain in the manufacturing, agriculture and services sector. These include:

- **Outsourcing**

Programmes will be implemented to nurture SMEs as Research and Development (R&D) partners. Collaborative ventures among Multinational Corporations (MNCs), Government-linked companies (GLCs) and SMEs will facilitate technology transfer and skills development and marketing;

- **Inter-firm linkages**

Creating business links between SMEs, GLCs and MNCs would enable SMEs to be more competitive and become reliable suppliers for global outsourcing networks which would expand Malaysia's trade with new export markets;

- **Entrepreneurship programmes**

Programmes, including advisory and outreach services, will be expanded to equip SMEs with new and improved management and business practices, methods in production, quality improvement, marketing and distribution; and

- **Knowledge skills**

Further development of technical skills amongst SMEs, especially in generating innovation and creating economic value from knowledge application.

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2. Third Industrial Master Plan (IMP3)

The priority accorded to developing domestic SMEs is further reiterated in the IMP3. The 15-year blueprint, published hand in hand with the 9MP, has outlined five clear strategies to support the development of diverse and competitive SMEs. The five strategies are:

i. Competitive Edge - Integration and Rationalisation

In order to enhance competitive advantage, SMEs are encouraged to integrate with MNCs, capitalising on the current outsourcing trends among large corporations especially in high value added activities. SMEs need to move up the value chain through rationalisation and specialisation, focussing on building and enhancing their core competencies, in order to compete regionally and globally.

Specialisation will in turn enable SMEs to better leverage on their core competencies in order to create a market niche in both domestic and overseas markets. SMEs will need to fully understand the market structure and customer needs in order to be flexible in adapting to changing demands and trends.

Efforts are already underway to assist SMEs in this aspect by placing SME employees at MNCs and through financial assistance in acquiring cutting edge technology. This includes “bridging technology” which combines several technologies and can help SMEs upgrade operations by providing a broader range of products or services.

The increased outsourcing trend amongst MNCs provides an excellent avenue for participation in the global market. To promote this further, the Government will intensify and strengthen inter-firm linkages with MNCs, enabling SMEs to become reliable and competitive suppliers. Currently, the Industrial Linkages Programme (ILP) under the Ministry of International Trade and Industry (MITI) is confined to the production phase of the manufacturing sector. This will be widened to cover the entire value chain for both the manufacturing and the services sectors.



The adoption of best business practices and benchmarking is key, for any business, in the ongoing effort to remain competitive. To this end, benchmarking programmes provided by the National Productivity Corporation (NPC) are promoted through industry associations and chambers of commerce. The Benchmarking On-line Networking Database (BOND) is a database of best practices and performance measurements set up by NPC to assist organisations in undertaking benchmarking activities.

(For more information, please refer to www.npc.org.my)

Shared Services and Outsourcing

To help realise Malaysia's potential, the Government will undertake international promotions to brand Malaysia as a major global hub for shared services and outsourcing (SSO) and increase awareness of Malaysia's competitiveness. Incentives will also be given to MNCs in Malaysia, such as tax exemptions on revenue from SSO, which can serve as a significant customer base for local outsourcing service providers to develop world-class competencies and large scale operations.

ii. Outward Bound - Armed and Prepared in a Global Arena

With the advent of a more liberalised market, SMEs can no longer rely on domestic demand. An expanded market provides new opportunities and greater export opportunities to capable SMEs. Financial institutions are urged to support domestic businesses, including SMEs, in their ventures overseas. This will go hand in hand with efforts from various Ministries and Agencies, such as the Ministry of Domestic Trade and Consumer Affairs (MDTCA), Small and Medium Industries Development Corporation (SMIDEC), Malaysian External Trade Development Corporation (MATRADE) and Multimedia Development Corporation (MDeC), who will initiate closer bilateral cooperation with foreign counterparts as well as promote industry linkages, joint trade commissions and exhibitions to facilitate networking between local and foreign SMEs. In 2006, nearly 1,000 SMEs benefited from business matching and enhancement programmes for example, the ILP.

For successful penetration into overseas markets, SMEs also need to be equipped with knowledge and skills in financial management and marketing. Ongoing programmes designed to enhance entrepreneurial capabilities have been expanded to include negotiation skills, merchandising, pricing, brand building and consumer behaviour. To further aid SMEs in this area, an interactive portal, MITI and Agencies Trade and Industry Information Exchange (MATRIIX), was developed to provide information on market intelligence such as consumer preferences, international standards and regulations, and environmental requirements. Plans are underway to introduce real time market information from other Agencies.

It is crucial for SMEs to conform to international standards and regulations for successful expansion to overseas markets. To ensure this, SMIDEC will collaborate with the necessary regulatory bodies to help SMEs conform to international standards and regulations. This is especially relevant for success in the Halal arena, a new and exciting growth area highlighted in the 9MP.

The global Halal food business is currently worth RM2 trillion and is expected to reach the RM6 trillion mark by 2010. This has initiated Malaysia's move towards becoming a Halal Hub by 2007, providing an opportune area for overseas expansion. To hasten this process the Halal Industry Development Corporation (HDC), was set up in 2006. With RM100 million allocated, the HDC will oversee the development of the Halal industry. Incentive packages in the development of the Halal Hub has been enhanced with RM20 million allocated to the SME Bank to help entrepreneurs develop Halal products.

(Please refer to Chapter 8 for more information on Halal Hub)

iii. ICT - Friend Not Foe

In line with global trends, growth amongst domestic SMEs will inevitably be driven by technology and innovation. The emergence of new technologies and products has influenced the way business is now conducted. As such, high priority has been given to strengthening technological capabilities of SMEs, with a total allocation of RM12.9 billion being set aside for information and Communications Technology (ICT) under the 9MP. Government agencies such as the Malaysian Technology Development Corporation (MTDC), MDeC, SMIDEC and the Malaysian Biotech Corporation (MBC) will collaborate to introduce technology foresight programmes to allow SMEs to take advantage of available technology.

To further promote research and development (R&D), collaborative ventures will be encouraged among MNCs, GLCs and SMEs to facilitate technology transfers and skills development and marketing. To further aid this endeavour, closer collaboration with Government institutions and universities are to be promoted through the Technology Development Cluster Programme set up in 2006 to help SMEs to undertake the commercialisation of potentially viable R&D results.

Technopreneur development will be expanded to support science and technology based SMEs, particularly Bumiputera SMEs, to benefit from home grown technologies. Measures to be undertaken include the provision of appropriate infrastructure, transfer of technology and improved access to financing.

Ultimately for any business to thrive, a conducive environment with supportive regulatory and institutional framework needs to be created. To achieve this an industry driven National SME Focal Point, involving entrepreneurs, research institutes, financiers, venture capitalists and relevant Government agencies, will be established for the exchange of information including new market and technology trends. Also launched in 2006, was the SMEinfo portal providing information on all aspects of SME development including financing, training and support.

(For more information please log onto www.smeinfo.com.my)

With the advent of a more liberalised market, SMEs can no longer rely on domestic demand. An expanded market provides new opportunities and greater export opportunities to capable SMEs

iv. Cohesive and Supportive Framework - Encouraging Potential to Shine

In order to achieve a higher rate of success, the approach has to be systematic and coordinated. This synchronised approach is to be carried out alongside financial support programmes to:

- Assist potential entrepreneurs to upgrade technical and professional skills;
- Assist in the purchase of new machinery and equipment;
- Provide industrial sites and special parks at competitive prices;
- Provide assistance in the registration and patenting of intellectual property (IP); and
- Reduce red tape for faster processing.

Greater support will be on offer through more inter-agency coordination in order to mobilise resources and obtain synergies for the overall development of SMEs.

v. Nurturing the Services Sector - Towards New Areas of Growth

The Census of Establishments and Enterprises 2005 has indicated that a significant 86.5% of SMEs are in the services sector. In order to tap into this burgeoning sector several areas for growth have been highlighted within this category. They include:

- Distributive trade - increasing new products and services for franchising;
- Business and professional services - encouraging entrepreneurs in specialist skills such as pharmacies and dental clinics;
- Logistics services - increased SME participation in the integrated logistics supply chain;
- Construction and related services - SMEs are to be encouraged to link with large construction companies to form strong domestic sub-contracting base to secure contracts locally and overseas; and
- Information and Communications Technology - to foster and stimulate growth of more ICT technopreneurs and SMEs by providing seed and start up funding.

With the increased allocation of resources outlined in the 9MP and IMP3, the Government has demonstrated its strong commitment for the development of efficient and competitive SMEs; a commitment that is more significant than ever as Malaysia moves towards realising its objective of becoming a developed nation.

Productivity Performance of SMEs in The Manufacturing Sector



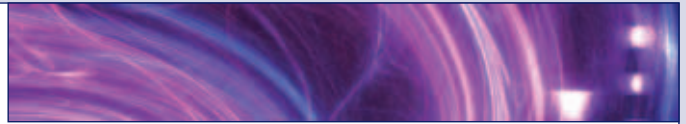
Small and medium enterprises (SMEs) in the manufacturing sector continued to perform well in 2006 with a growth rate of 7.4% in value added to RM17.8 billion. Concurrently output grew from RM82.0 billion to RM88.3 billion or 7.7% while employment rose from 394,670 to 402,496 or by 2.0%.

Total Output, Value Added and Employment of SMEs in 2006

	Value Level*		Percentage Share of Manufacturing Sector (%)		Growth (%)
	2005	2006	2005	2006	2006
Total Output	81,990	88,266	29.6	29.8	7.7
Value Added	16,576	17,798	25.9	26.0	7.4
Employment	394,670	402,496	31.3	31.3	2.0

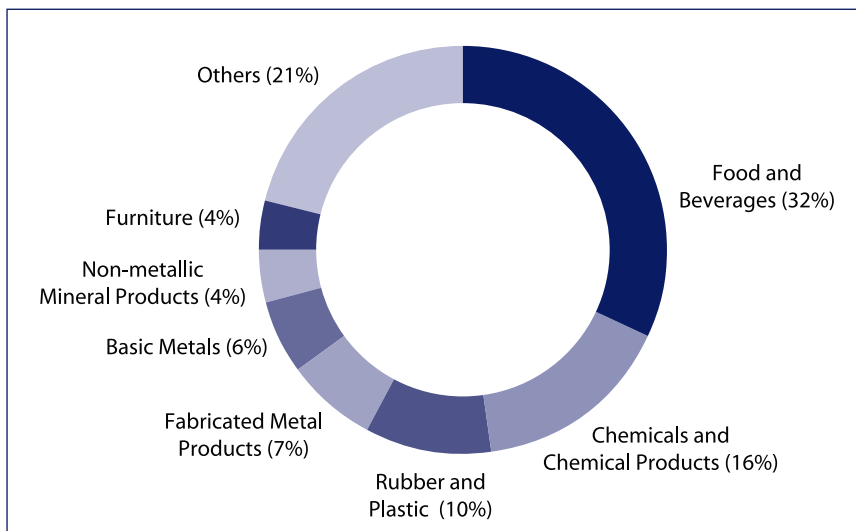
* Value Level for Total Output and Value Added are in RM Million

Source: Computed by National Productivity Corporation (NPC) from Annual Survey of Manufacturing Industries, Department of Statistics, Malaysia, various issues



SMEs account for 96.5% (39,436), of all enterprises in the manufacturing sector. The majority are engaged in the food and beverages sub-sector (32.5%), followed by chemicals and chemical products (15.6%), rubber and plastic products (10.3%) and fabricated metal products (6.6%). These industries accounted for 79.0% of total SME output, 29.8% of total manufacturing output, 26.0% of total value added and 31.3% of total manufacturing employment.

Distribution of SMEs in the Manufacturing Sector in 2006

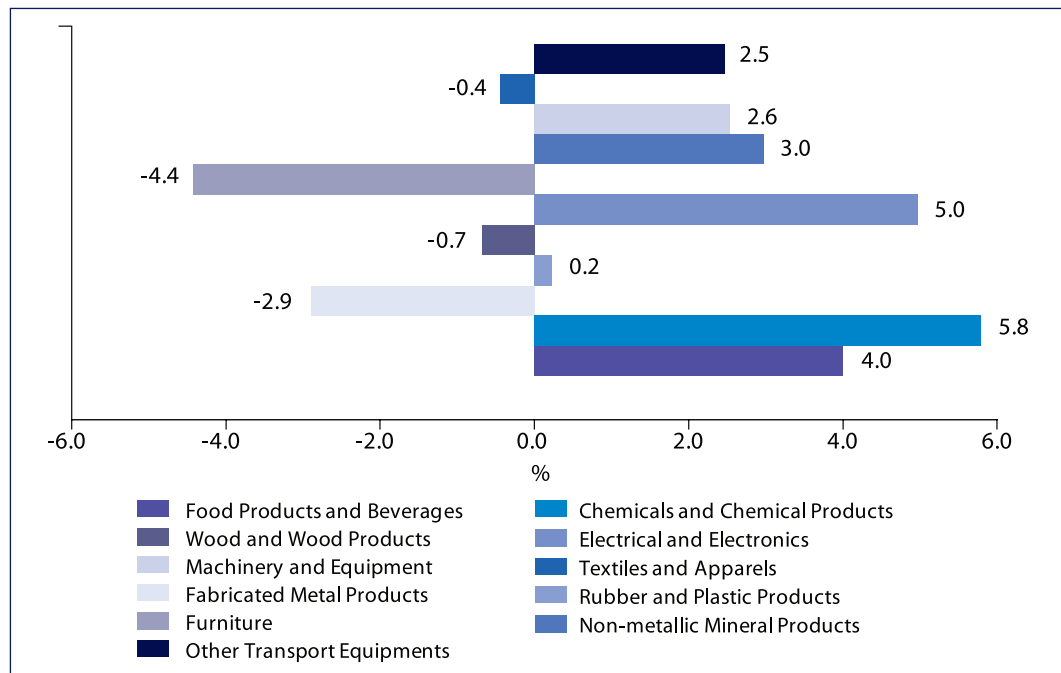


Source: Computed by National Productivity Corporation (NPC) from Annual Survey of Manufacturing Industries, Department of Statistics, Malaysia, various issues

A continuous rise in fixed asset investments, growing steadily by 2.7% to RM 37,000, indicates that SMEs are becoming more capital intensive. Investments in fixed assets has enabled SMEs to achieve a higher growth of 2.5% in capital productivity. Furthermore, high investments in infrastructure, new machinery such as precision machining and tooling, process and product engineering and automation, has improved SME capacity to produce products and services that meet global market requirements. Companies able to manage existing machineries efficiently recorded higher capital productivity indicating that SMEs were efficient in using resources to create value.

Despite contributing substantively to output and value added, wood-based products and furniture sub-sectors remained low in capital utilisation, a reflection of the labour-intensive nature of the industry. This was also the case in the labour dependent textiles and apparels sub-sector.

Capital Intensity in SMEs by Manufacturing Sub-sectors in 2006

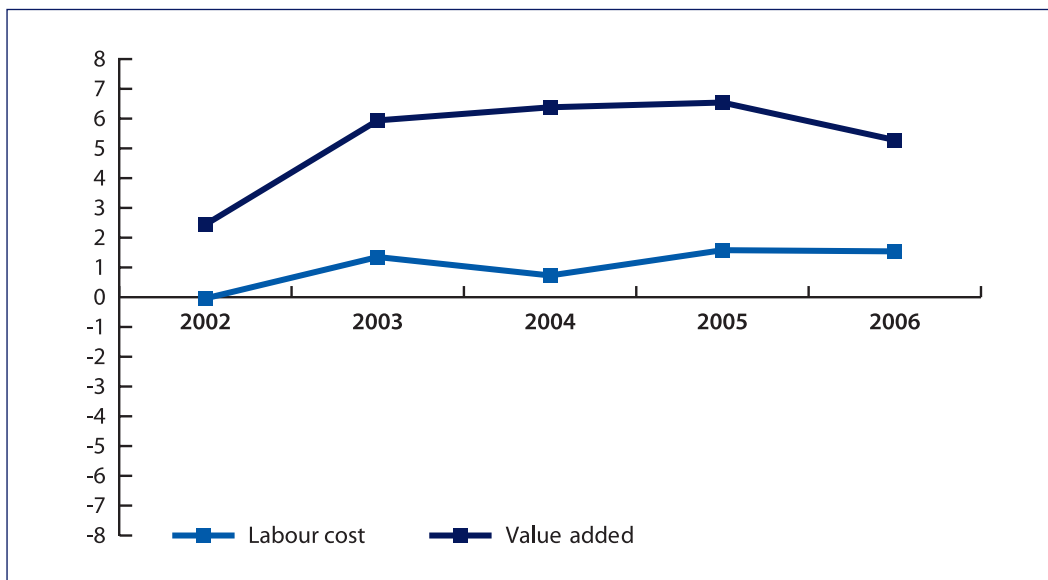


Source: Computed by National Productivity Corporation (NPC) from Annual Survey of Manufacturing Industries, Department of Statistics, Malaysia, various issues



Over the course of four years, SMEs have continued to sustain competitive labour costs with further improvements in 2006 reflected in a 3.8% reduction in unit labour cost. Sectors which registered improved labour costs included food and beverage, petroleum, chemical and basic metals industries. Initiatives to increase the efficiency in the utilisation, higher investments in infrastructure and machineries and expansion in capacity utilisation had helped SMEs improve their productivity and competitiveness.

Labour Cost Competitiveness of SMEs



Source: Annual Survey of Manufacturing Industries, Department of Statistics, Malaysia

Moving forward, SME productivity is expected to grow by more than 5.5%. In order to achieve this target, SMEs need to improve on several factors which include:

- Increased operational and cost efficiencies;
- Faster response to new challenges in the changing business environment, both domestically and globally;
- Embrace new technologies and adopt ICT in their core manufacturing functions;
- Proactive in the implementation of productivity and quality management systems; and
- Develop more skilled workers to meet the technological changes and higher market demand.