SMU

Publication: The Business Times, p 10
Date:3 July 2012
Headline: Why SMEs should aim at becoming exporters

Why SMEs should aim at becoming exporters

Q: Should SMEs aim to become exporters rather than serve only the domestic market? What are the benefits to SMEs in doing so? Does the smallness in size limit their productivity growth? Are there any channels for SMEs to get assistance from the authorities, and what are these?

A: Over the past two decades, economists have been able to study big micro-level sets of data of individual firms operating in both developed and emerging economies and to track their economic performance over several years. What has been learnt is that there is a great deal of heterogeneity; not all firms in a given industry are alike. In particular, among firms in any industry, the exporters are more productive than the non-exporters and they tend to pay higher wages to workers with similar characteristics.

For example, between any two workers with the same educational qualifications employed in the same industry, the one who works in a firm that sells its product both domestically as well as to foreign markets enjoys a wage premium over his or her counterpart who works in an SME that sells only in the domestic market. This is so because exporters, being more productive, are more willing to invest resources to screen workers to ensure a better job fit and derive a more able workforce capable of improving the firm's bottom line. They are also more willing to invest resources to provide training to their workers to enable them to be more effective in their jobs.

HOON HIAN TECK

Engage SMU profs

While many productive firms self-select into exporting, economists have found evidence that there is also "learning-by-exporting". In other words, once a firm is sufficiently productive to become an exporter, its access to export markets itself leads it to become even more productive over time. Partly, this has to do with being able to enjoy economies of scale. It also has to do with the fact that as these exporting firms become bigger, they find it worthwhile to invest in R&D. As a result, they generate productivity growth and become more efficient over the medium term to long term.

A question that an SME owner might ask is whether a firm's small size limits its ability to be productive and its ability to export. It is instructive to turn to Taiwan's experience to look for an answer as the economic growth of Taiwan – as an export-oriented economy since the early 1960s – was based mainly on SMEs.

There has been research on the economic performance of Taiwanese SMEs, particularly those in the manufacturing sector, to study whether it is higher productivity that leads to growth in firm size or the largeness of firm size that leads to higher productivity. It was found that, regardless of the firm size, those which were more productive survived and were more likely to grow bigger, eventually enjoying average productivity levels that converge with those of large firms.

In Singapore, Qian Hu Corporation Ltd is an example of a small-sized SME that transited from serving only the domestic market to becoming an exporter. In the mid-1980s, it started breeding guppies for sale locally but today it is a listed company that distributes a range of products to both local and overseas markets.

Assistance for SMEs

The Taiwanese experience suggests that financial incentives to boost productivity should not be targeted at SMEs of a specific size. Indeed, the Singapore government's main fiscal incentive package to help local SMEs improve their productivity – called the Productivity and Innovation Credit (PIC) scheme – is neutral to firm size. Beyond financial incentives to improve productivity, there is no doubt that the cultivation of an adventurous and innovative culture will also help more potential SME entrepreneurs to take the leap into launching new business ideas. The more creative among them will be able to catch the tide to expand their businesses, transiting from serving the domestic market solely to making inroads into overseas markets as well. As a result, they will earn higher profits and offer better pay.

Exporting to an overseas market requires an SME to incur a fixed cost – that is, to incur an expense that is independent of the number of units of the good that it actually sells. This may include, for example, paying for research to study overseas markets, not only of customer preferences but also of the set of trading rules that govern exports to that market. In newly emerging markets, the SME also has to gather information about the level of political risk. Accordingly, the SME has to be productive enough to earn sufficient profit to cover the fixed cost and absorb the risk. Efforts by government agencies in this regard – such as the Emerging Markets division of the Ministry of Trade and Industry as well as by International Enterprise (IE) Singapore, which help local SMEs to better understand the economic and political environment of potential overseas markets – will help to lower the fixed cost of exporting.

While the PIC scheme is not directly aimed at helping SMEs break into overseas markets, another government initiative is targeted at helping SMEs with their financing for long-term projects overseas. Announced during Budget 2012, this comes in the form of a specialised project finance company, put together by Temasek Holdings and expected to be operational in the second half of the year.

Evidently, if more of our local SMEs look towards the international marketplace and sell to foreign markets, not only will Singapore's GDP be boosted, local businessmen will also get to enjoy higher profits and more Singaporean workers can expect to find good jobs that pay a premium.

Hoon Hian Teck is a professor of economics and associate dean at the School of Economics, Singapore Management University

Brought to you by:

HAVE a pressing question about a business-related issue that your company is facing? Professors from the Singapore Management University (SMU) will provide their expert advice and answers to your queries on a fortnightly basis. All you need to do is send us an e-mail with your query at btnews@sph.com.sg and include particulars such as your name, designation and company.

If you do not want your name or company's details to be published, please indicate so and we will leave them out when we go to print. Please also mention "Engage SMU Profs" in the subject line of your e-mail. Start firing those questions today!

Source: The Business Times © Singapore Press Holdings Limited. Permission required for reproduction.