

## Chapter 5. Conclusions and Policy Recommendations

Although it is difficult to establish common trends in the diversified universe of SMEs, the case studies conducted in several OECD member and non-member economies provided some new insights on the performance of SMEs in global value chains. One result that stands out from the different findings across sectors is that successful participation in global value chains brings stability. Small firms that are able to remain in value chain(s) despite keen global competition, or SMEs that succeed in ‘jumping on board’ normally gain stability and even expand their business. This is often accompanied by the upgrading of technological and human capital, as a result of the greater exposure and facilitated access to information, business practices and technologies that SMEs experience in GVCs. Indeed, co-operation with the network appears a key factor in facilitating the upgrading process. Case studies in the automotive and tourism sectors indicated that co-ordination with upstream and downstream partners increases the chances of success of small firms in the value chain. This seems related to substantial benefits in terms of status, information flows and learning possibilities. Successful SMEs in GVCs acquire more autonomy from their larger counterparts and increase opportunities to grow further by leveraging on access to an extended network of partners and to superior technology and improved staff skills.

The increased opportunities for SMEs come with serious challenges in terms of managerial and financial resources, and ability to upgrade, to innovate and to protect in-house technology. When questioned on these issues, SMEs point to their lack of ability to support adequate R&D, training of personnel to comply with the strict requirements of product quality standards. Insufficient working capital, caused by delayed payments from international partners, is also a barrier to the participation in GVCs. Moreover, if upgrading a small firm’s position in the value chain is possible, it is typically linked to the take-up of a larger and more complex set of tasks. In the case of a small supplier, this would include the manufacturing of a product or the provision of a service, as well as contributions to product development and organisation and monitoring of a network of sub-suppliers to ensure delivery and quality at competitive costs. The lack of SMEs’ awareness of the complexity of the issues plays against their possibility of responding timely and effectively to the challenges of globalisation.

Governments could facilitate SME gainful participation in global value chains through policy initiatives in specific areas:

- ***Awareness-raising of the potential of participation in global value chains.*** Many SMEs that are used to serving local markets may find it difficult to gain a good understanding of the advantages and potential of subcontracting. This also applies to the potential for SMEs to subcontract abroad part of their production, in order to improve their competitiveness through rationalisation of resources. Although the diffusion of ICT has made market intelligence easier also for SMEs, their limited resources and lack of managerial capacities still hamper accurate information and analysis on the opportunities in foreign markets.

- **Increasing participation in global value chains** through initiatives such as the facilitation of SME consortia for joint marketing or for entering joint bids, particularly in government procurement, or promotion schemes for potential suppliers.
- **Supplier financing.** Gainful participation in value chains often requires substantial investments to acquire or develop superior production technologies and logistics systems, invest in human capital, or certify newly required standards. Moreover, suppliers normally receive incoming payments from their customers several weeks or even months after the delivery of orders and contract enforcement and collection of payments may be a significant challenge for an SME. Policies aimed at improving SMEs' accounts receivables and facilitating SME financing can help small subcontractors overcome liquidity problems, *e.g.* by contributing to the development of financial schemes such as factoring.
- **Promotion of technological upgrading** is critical in order to encourage SMEs to capture more value added from participation in global value chains. Policy in this area should aim to support training and capacity building via skill development programmes; promote partnerships between SMEs and organisations overseas that can develop or transfer technology, products, processes or management practices; and to facilitate the technological upgrading through various financial schemes, such as credit lines for upgrading.
- **Insufficient protection of intellectual property.** The protection of intellectual property rights is of high relevance to SMEs. As discussed, the insufficient protection of SMEs' intellectual property rights in international markets is already having harmful effects on those small subcontractors that experience unfair business behaviour by their customers. The negative impact is twofold. In addition to the direct damage created by deceptive business practices, small firms' incentives to innovation may well be reduced if appropriation of economic benefits is threatened. Governments should consider including provisions for technology transfer from small subcontractors to MNEs within the OECD Guidelines for Multinational Enterprises (MNEs). At present, these Guidelines only cover the transfer of technology and the need for protection of intellectual property rights from multinational enterprises to other partners, as it is considered that MNEs are the main conduits of technology transfer across borders (*Section VIII, Science and Technology*, OECD Guidelines for MNEs, Revision 2000).
- **Harmonization of compliance procedures.** The adoption of product and process standards has several well-known benefits for firms. It enables them to introduce new technology and integrate business practices that improve their overall performance. However, different and concurrent standards can become barriers to transmission of information and to trade. Also, the costs of compliance with standards are proportionally too high for small firms. The problem is aggravated when these firms have to cope with an increasing number of private standards set by customers in addition to mandatory ones. Governments should ensure that national certification systems do not impose an excessive burden on small firms and encourage SME participation in the standard-setting process. Initiatives such as group certification for small firms in local regions might also prove effective, if trust in the control mechanisms can be gained.

- **Promotion of skills development.** Effectiveness of aforementioned policy measures, to a certain degree, is contingent on having skilled human resources in SMEs. Participation in global value chains can accelerate SMEs' upgrading of human and technological resources, through technology and knowledge transfer and implementation of new business practices. Conversely, participation may be demanding as well, to the extent that a threshold of capabilities could be necessary to successfully enter value chains. Policies that aim at raising technical and managerial skills in SMEs can facilitate integration of these firms into global chains.
- **Attracting foreign direct investment.** FDI promotion policies may facilitate the integration of firms in global supply chains. Some policies can explicitly be designed to attract MNEs that would promote technology and knowledge transfer to local suppliers and subcontractors, whereas others may aim at helping established foreign affiliates to enter and/or upgrade into higher-value activities. After-care services for foreign investors are important and can influence them to develop business linkages with SMEs.
- **Promoting the development of industrial clusters.** Cluster initiatives allow for economies of scale and agglomeration and also help developing an experienced local pool of skilled labour and a network of firms co-operating in complementary areas of specialisation. By doing so, they strengthen their competitive advantages in a sustainable manner and become attractive sites for quality FDI. In many cases, the presence of MNEs becomes crucial to integrate clusters into GVCs, and to strengthen their export capacity both from the production and distribution point of view.
- **Promoting the development of domestic industries and service networks in developing countries.** Such networks would be able to link effectively with international production networks, by promoting entrepreneurship and enhancing competitiveness at firm level through technology and business linkages. This calls for using official development assistance (ODA) more effectively to support developing countries' efforts to undertake a wide range of proactive measures to promote trade and investment in an integrated way. At the multilateral level (WTO) it is necessary not only to promote a country's capacity for trade policy formulation and negotiation but also to enlarge the scope of Aid for Trade so that it assists countries to build their productive capacity.

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