



Role of SME policies in fostering inclusiveness in ASEAN

ASEAN SME POLICY INDEX AS A TOOL TO PROMOTE INCLUSIVENESS



***ROLE OF SME POLICIES IN FOSTERING
INCLUSIVENESS IN ASEAN***

ASEAN SME Policy Index as a tool to promote inclusiveness

***ROLE OF SME POLICIES IN FOSTERING
INCLUSIVENESS IN ASEAN***

ASEAN SME Policy Index as a tool to promote inclusiveness

February, 2018

Paris

The opinions expressed and the arguments employed herein do not necessarily reflect the official views of OECD countries, nor ERIA or ASEAN.

This document, as well as any data and any map included herein, are without prejudice to the status of or sovereignty over any territory, to the delimitation of international frontiers and boundaries and to the name of any territory, city or area.

Foreword

The objective of the paper is to provide a distinctive contribution to the discussion about how to achieve inclusive and sustainable growth in the countries of the Association of South East Asia Nations (ASEAN), by focusing on the role played by Small and Medium Sized Enterprises (SMEs).

The paper has been jointly prepared by the Organisation for Economic Co-operation and Development (OECD) and Economic Research Institute for ASEAN and East Asia (ERIA) on the occasion of the Ministerial Conference “Inclusive ASEAN”, jointly organized by the Ministry of Foreign Affairs of Japan and the OECD and held in Tokyo on 8-9 March 2018. It has benefited from feedback from the ASEAN Coordinating Committee for Micro Small and Medium Enterprises (ACCMSME).

This note was written by Mr Antonio FANELLI, Senior Economist, Global Relations, at OECD, with substantial inputs from Mr Dionisius A. NARJOKO, Senior Economist, ERIA.

The paper draws on inputs from a number of reports recently produced by the OECD and ERIA on the topics of SME policy, economic development, Global Value Chains (GVCs), women entrepreneurship and productivity dynamic in ASEAN. In particular the paper presents a methodology for the upcoming ASEAN SME Policy Index 2018 report jointly conducted by ERIA and the OECD in cooperation with the ASEAN Coordinating Committee for Micro Small and Medium Enterprises and the support of the Government of Canada.

Table of contents

Foreword	4
Executive summary	6
1. Introduction	9
2. Main characteristics of the SME population in ASEAN	10
3. SME policy as an economic and social development tool	15
4. Three approaches to support inclusiveness through SME policy in ASEAN.....	19
Conclusions: common and divergent themes.....	24

Tables

Table 2.1. SME Definition per AMS.....	10
Table 4.1. Trade data in AMS per country	20

Figures

Figure 2.1. Labour productivity growth in Emerging Asia	11
Figure 2.2. Multi-factor productivity growth in Emerging Asia	12
Figure 4.1. Expert evaluation of ASEAN framework conditions for entrepreneurship	22

Boxes

Box 3.1. The SME Policy Index : Objectives and Methodology	17
Box 3.2. The ASEAN SME Policy Index 2018 as a way to benchmark SME Policies	18
Box 4.1. Promotion of Sustainability in ASEAN.....	23

Executive summary

ASEAN has exhibited a strong economic growth performance over the past three decades, supported by a steady supply of increasingly better-educated workers; a process of capital accumulation facilitated by a high domestic savings rate; healthy FDI and foreign capital inflows; the absorption and diffusion of new technologies; and by the utilisation of the region's vast natural resources endowments. However, this growth has not always translated into inclusive development patterns across and within the countries.

SME development could play an important role in fostering inclusive growth over the mid- to long-term. An effective SME policy would benefit from a better understanding of the main characteristics of SMEs across ASEAN member states. SME definitions vary across the region and globally, but SMEs still constitute the vast majority of active enterprises accounting for 97 to 99% of total registered enterprises in most economies. Second, the SME population is typically highly diversified – in terms of size, ownership typology, sector, level of integration in domestic and global value chains – though two types of enterprises have the highest chance of contributing to economic growth: high growth enterprises, and innovative start-ups. Finally, most ASEAN Member States (AMS) host a substantial share of informal enterprises, mainly micro-sized. These enterprises can be classified as informal either because they remain unregistered or because they are not fully compliant with all regulatory requirements, even if they are in some sense “known” to the authorities.

There are a number of challenges that SMEs face across ASEAN, attributable to different phenomena including the changing landscape for international trade, a lack of resources to strengthen productivity, and the digitalisation and atomisation of manufacturing industries. Yet these developments have also brought new opportunities, for instance via integration into global value chains. The AMS are highly integrated into global value chains and often SMEs are strongly engaged as direct suppliers of intermediaries, hence GVCs may provide new opportunities for developing the economic activity of SMEs. An important element of SME internationalisation takes place through indirect exports – SMEs rely on larger national or multinational firms to engage in GVCs.

A number of AMS are increasingly using SME policy as a tool to promote economic and social development. Policymakers tend to have three different approaches to SME policy, including a) *SME policy as a tool ensuring market efficiency and that all enterprises have equal access market access conditions;* b) *SME policy as a structural challenge that requires targeted pro-active government intervention;* c) *SME policy as a tool to achieve better social development.*

Generally, the AMS adopt an open policy-mix, combining elements from those three different approaches or adopting different approaches for different segments of the SME population with various levels of intensity. Each AMS has its own pace for integrating the issue of inclusiveness and has different issues they are focusing on. This paper identifies three approaches to SME policy through which AMS support inclusiveness in ASEAN. They include:

- 1 Enhancing SME economic integration at the sub-national, regional and global level.** The prevailing economic growth model in the ASEAN region plays a strong emphasis on the integration into global value chains and on the development of export-oriented activities. Most AMS show strong trade growth during the last ten years. Faster export led economic growth contributes to generate new and better jobs, as export oriented enterprises are usually more productive than companies oriented towards local market and more likely to operate in a formal way. If export led growth is also associated to economic diversification, the productive base can be broadened and more resources to finance human capital development through skill enhancement and better education can be generated, thereby contributing to more inclusive growth. When looking at public policy measures supporting GVCs integration and linkages with large enterprises a group of AMS (Indonesia, Malaysia, Singapore, Thailand and Viet Nam) stands out for the intensity and the quality of their initiatives. Some AMS also promote SME greening or sustainability promotion initiatives as a way to facilitate access of green products into GVCs. Those countries are the leading manufacturing hubs and GVC integration is crucial in supporting industrial growth. Finally, the dynamism of e-commerce in South East Asia has attracted significant amount of investment and a large number of e-commerce and e-business platforms are operating in the region.
- 2 Diffusing and supporting entrepreneurship through innovation policies.** High-growth and innovative enterprises play a crucial role in fostering the development of a country enterprise sector, by ensuring that enterprise competition dynamic remains vibrant, by spurring productivity gains, by fostering technological upgrading and by generating new employment opportunities. As innovative and high-growth enterprise tend to concentrate in highly integrated hubs, their development may also increase geographic inequality within a country. But their contribution to economic growth, quality of living, widening of opportunities, is likely to compensate the negative impact on equality. The latest GEM report on ASEAN shows (GEM 2016) that framework conditions for high-growth entrepreneurs in ASEAN are relatively good. Innovative hubs have been established in several ASEAN cities, such as Singapore, Jakarta, Kuala Lumpur and Bangkok. However, SME productivity remains substantially lower than that of larger enterprises, but there are indications that the gap may start to shrink and already some of the SMEs operating in advanced service sectors have achieved high productivity records. Also, while the most advanced AMS are moving closer to the technological frontier and they have put in place effective innovation supporting eco-systems, the less developed AMS are still engaged in early stage institutional development, while facing a lack of financial and human resources to support policy actions.

- 3 **Enhancing economic opportunities amongst marginalised groups.** Entrepreneurship promotion takes on a distinctly social approach in majority of AMS, and SME policy is predominantly used as a means to fulfil social policy objectives. AMS in many cases have developed dedicated policies for specific target groups such as women, youth, and persons with disabilities. Specifically for women, all AMS have agencies and coordination mechanisms to advance women entrepreneurship and enhancing women's economic activity has been widely acknowledged as a general aim in national strategies.

In summary, it is noted that ASEAN as a region has achieved remarkable progress on tackling the issue of inclusiveness through SME development over recent years.

The ASEAN SME Policy Index 2018 which is currently being developed could provide a useful tool for benchmarking relevant policies to further enhance inclusiveness. Its findings, once launched in 2018, could help policymakers to fill information gaps and to have a better understanding of how their country's SME framework differs from that of their neighbours.

Moving forward, the AMS could further focus on strengthening monitoring mechanisms and increasing the volume of data available – both on the performance of SME policies as well as the performance and characteristics of active SMEs operating in their respective countries. Through use of this data, policymakers would be able to acquire a better understanding of the current status of SME development within their countries, and, supplemented by additional tools such as the ASEAN SME Policy Index or SME Policy tracking tools, identify gaps in order to develop more tailored policies.

1. Introduction

The ASEAN economic community has experienced a prolonged period of high economic growth since the process of enlargement was completed in 1999, and for many countries this trend can be observed since the late 1970s. This period of long-term economic growth has been supported by a steady supply of increasingly better-educated workers; a process of capital accumulation facilitated by a high domestic savings rate; by healthy FDI and foreign capital inflows; by the absorption and diffusion of new technologies; and by the utilisation of the region's vast natural resources endowments. In particular, and specific to ASEAN, this phenomenon has been facilitated by a high level of integration in global value chains (GVCs) and trade liberalisation, enabling ASEAN firms to increase their competitiveness as exporters – in 1995 the share of foreign value added (imports) used to produce exports (the buying element of GVCs) reached 29%, increasing to 33% by 2011. Recently ASEAN firms have started to increasingly source their inputs from regional providers, particularly those within the Asian Productive Network, replacing traditional providers in the European Union and the United States.

ASEAN member states (AMS) have been going through a process of rapid change, economic growth and a number of structural challenges. ASEAN as a region produced a remarkable progress with tackling issue of inclusiveness over the last years. The process of integration and the 2015 ASEAN Economic Community (AEC) Blueprint 2025 showcases ASEAN's aim to develop an inclusive, resilient, people-oriented, and people-centered community.

Although there has been progress, AMS still confront issues related to inclusiveness. There are three types of economic diversity or inequality across ASEAN. The first is *inequality of income distribution across member countries*, which reflects different levels of economic development, as well as different levels of factor and natural resource endowment. The second is income *inequality within individual countries*. The third type is divergence of economic opportunities for often marginalized groups of the population – a type of *inequality within individual countries that requires a targeted rather than a horizontal response*. Finally, although not limited to three types of inequality, other important elements still play an important role such as the *sustainability element*, or inequalities of resource access between present and future generations, as well as access to the physical infrastructure.

This note will explore the role that SMEs and SME policy could play in fostering inclusive growth over the mid- to long-term. It will start by describing the main characteristics of its SME population. It will then address how each type of inequality can be addressed through a subset of SME policies. It will conclude with suggestions on how a higher level of inclusive growth can be

promoted through SME development policies. This note does not present the initial findings from the ASEAN SME Policy Index 2018.

2. Main characteristics of the SME population in ASEAN

Across countries at all levels of development, SMEs are key players in promoting economic growth, inclusiveness and sustainability. SME definitions vary throughout ASEAN (See Table 2.1) and also globally, but across most economies SMEs constitute the vast majority of active enterprises, with large enterprises accounting for less than 1% of all registered enterprises (UNESCAP, 2014). The majority of active enterprises (65 to 75%) are micro-enterprises, and this share substantially increases where sole entrepreneurs – including those engaged in subsistence farming – are also included as micro enterprises in SME statistics. Generally micro enterprises are defined as firms with up to ten employees. Small enterprises take second place, accounting for around 20% of the enterprise population, followed by medium-sized enterprises, which generally account for no more than 5-10% of the total population.

Table 2.1. SME Definition per AMS

Country	Type		Criteria			Sector approach		Upper threshold*
	Legal	Working	Employment	Assets	Turn-over	Cross-sectorial	Sector-specific	
Brunei Darussalam		✓	✓			✓		100
Cambodia	✓		✓	✓		✓		200
Indonesia	✓			✓	✓	✓		–
Laos			✓	✓	✓		✓	99
Malaysia	✓		✓		✓		✓	200 (M) / 75 (S)
Myanmar	✓		✓	✓	✓		✓	300 / 600* (M)
Philippines	✓			✓		✓		–
Singapore		✓	✓		✓	✓		200
Thailand	✓		✓	✓			✓	200
Viet Nam	✓		✓	✓	✓	✓		200

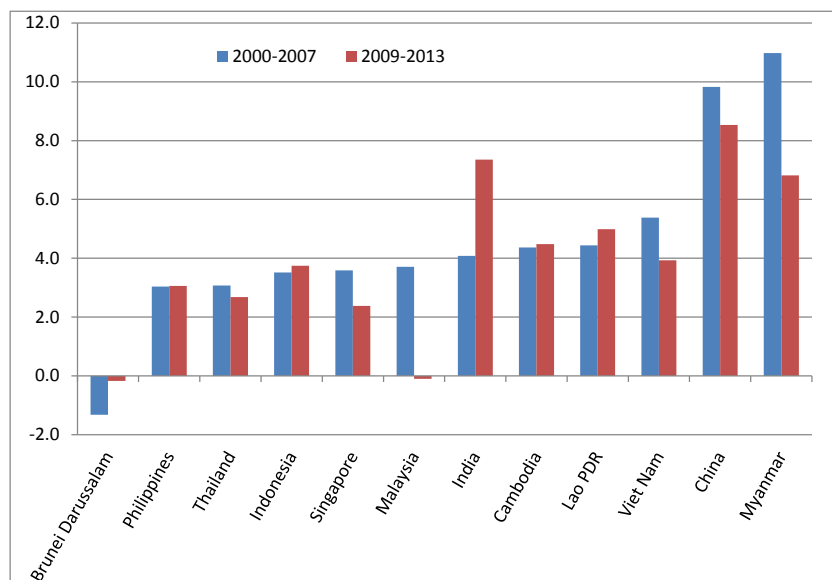
*Note: *For employment*

Source: National legal statements from AMS.

In terms of their contribution to aggregate employment, SMEs generally account for a large share of private sector jobs, ranging from 60 to 70% in OECD countries. Yet they generate a significantly lower share of value-added in manufacturing (OECD, 2017a). In the OECD, this is not generally the case for services, where they generally benefit from their proximity to the end-customer and more flexible structure, and do not require the same economies of scale and access to capital resources that benefit manufacturing activities.¹ In OECD countries this contribution – both to aggregate employment and the generation of value-added – has increased over recent years, largely due to larger-firm downsizing and increased outsourcing, as technological developments reduce the importance of economies of scale, facilitate the development of business and service networks and foster the creation of an eco-system that supports small-scale entrepreneurship whilst increasing the demand for specialised and high value-added services.

Over recent decades developments in communication technologies combined with falling trade costs have facilitated the fragmentation of production across countries and the rise of Global Value Chains (GVCs), allowing ASEAN economies to become increasingly integrated into GVCs (OECD, forthcoming). Production has become increasingly complex with value added crossing borders several times, combining the inputs of goods, services and intangibles of several firms along the way (OECD, 2013; DeGain et al, 2017a). Productivity growth in the four years following the global financial crisis and its immediate aftermath (2010-13) has tended to be lower than in the four years preceding it (2004-07), except for multi-factor productivity (MFP) growth in Indonesia, the Philippines and Thailand, and labour productivity growth in Brunei Darussalam, Cambodia, India, Indonesia, Lao PDR and Thailand (OECD, 2017a). Performance has varied across sectors, and there has been some evidence of faster growth in lower-productivity sectors in recent years. (OECD, forthcoming).

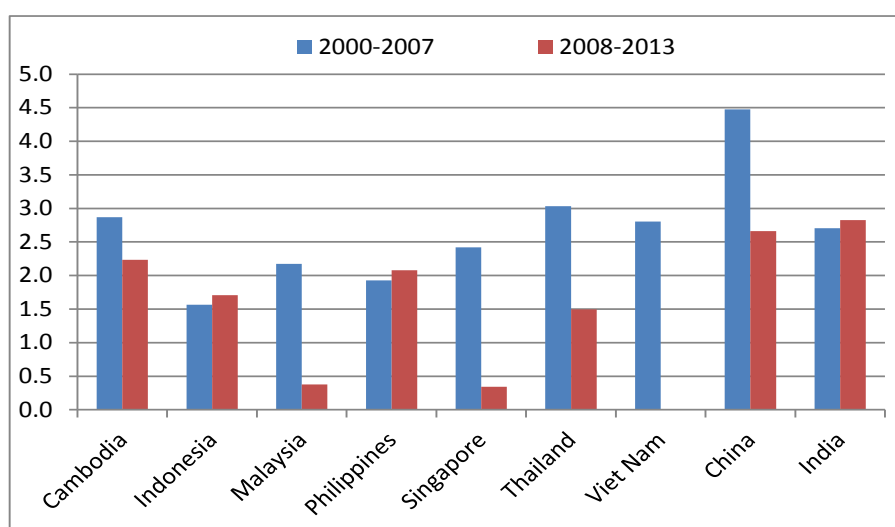
Figure 2.1. Labour productivity growth in Emerging Asia
(Annual growth in labour productivity, 2000-2007 and 2008-2013)



Source: APO (2015), *APO Productivity Database 2015*, www.apo-tokyo.org/wedo/measurement.

¹ SMEs are estimated to account for 60% or more of total value added generated in services across the OECD.

Figure 2.2. Multi-factor productivity growth in Emerging Asia
(Annual growth in multi factor productivity, 2000-2007 and 2008-2013)



Note: MFP data not available for Brunei Darussalam, Lao PDR or Myanmar.

Source: APO (2015), *APO Productivity Database 2015*, www.apo-tokyo.org/wedo/measurement.

SMEs are challenged by the changing landscape for international trade, but also have important new opportunities to contribute to greater engagement of SEA economies in global value chains, e.g. thanks to digital technologies. Strengthening productivity growth is another important challenge for SMEs. Recent OECD work has pointed to a growing gap between global productivity leaders (often large, multinational firms) and lagging firms (often smaller, domestic firms). An important question is the extent to which SMEs in SEA can benefit from ongoing technological changes in the global economy and strengthen their productivity performance, or whether they risk falling behind, as appears to be the case with SMEs in some OECD economies (OECD, 2015) through further integration into GVCs.

The SME population is typically highly diversified, in terms of size, ownership typology, sector, level of integration in domestic and global value chains, amongst other characteristics. However, two specific types of enterprises are increasingly being studied as having an important role in driving increased competition and economic development: *high growth enterprises*; and *innovative start-ups*. Those two typologies represent a small percentage of the total SME population, but they are crucial to the establishment of a vibrant, competitive and innovative SME sector, a goal pursued by government in developed and emerging economies.

There is not much statistical evidence of the performance of high-growth and innovative start-ups, but anecdotal evidence is quite significant. In particular a number of innovative and technological based start-ups from the region have been labelled “unicorn” firms, including *Garena*, *Lazada* and *Razer* (Singapore); *GrabTaxi* (Malaysia); *Tokopedia* and *Traveloka* (Indonesia); and *VNG* (Viet Nam). The rapid spread of technology incubators across the region is also indicative of strong market potential for start-ups in the region.

The characteristics of the population in ASEAN countries are very much in line with the stylised facts presented above. According to official national statistics SMEs account between 97 and 99% of registered enterprises in all AMS, with the exception of Myanmar (87%), where data is scarcer.² In terms of private sector employment, they generally account 61 to 97% of the total, with micro-enterprises accounting for the highest share of establishments and employment in all countries except Cambodia, where most formal employment is concentrated in medium-sized enterprises, predominantly in the highly labour-intensive garment sector. In terms of contribution to GDP, data is scarce, but the figure ranges from 61% in Indonesia (with the caveat that this figure is particularly high because the country counts independent farmers as micro enterprises, and as a result this group accounts for 99% of all enterprises) to 16%¹ in Brunei Darussalam, an economy dominated by a large oil and gas sector (DEPD, 2015).

Where sectoral data are available, it appears that ASEAN SMEs mostly operate in the service sector. In the Philippines only 12.7% of the SMEs operate in manufacturing, whilst 46.5% are engaged wholesale and retail trade and another 13.3% operate in the hospitality sector (as providers of hotels, restaurants, and similar services). In Myanmar, SMEs are to be principally found in the food and beverages sector, accounting for 63% of all SMEs. Viet Nam is an exception to this trend, with 43% of the SMEs engaged in manufacturing operations and a considerable share of these firms integrated into global value chains. Vietnamese SMEs, along with FDI, have been one of the key drivers in turning the country into a major manufacturing hub in Southeast Asia, whilst state owned enterprises have continued to dominate heavy and basic industry, natural resources and utilities.

As previously mentioned, the AMS are highly integrated into global value chains. According to a study recently conducted by the OECD (2016) on the integration of manufacturing SMEs from four AMS (Singapore, Thailand, Indonesia and Viet Nam) into GVCs, SMEs are strongly engaged as direct suppliers of intermediaries. In Thailand 16% of direct exports used for further processing abroad are produced by SMEs, compared to 6% generated by larger enterprises. In general the findings from these countries suggest that regional SMEs mostly participate in GVCs as suppliers to larger firms than as producers of direct exports.³

² In this country, SME data is only available for firms registered with the Ministry of Industry, and restricted to firms operating in industrial zones.

³ In Viet Nam, for instance, direct exports account for 14% of total export products generated by manufacturing-SMEs, whilst indirect exports through larger firms account for 20%.

Finally, SMEs in ASEAN are also constituted by informal enterprises. Those include enterprises that are not formally registered (total informality) as well as enterprise that are formally registered, but not fully compliant with all regulatory requirements. Informality is widespread across Southeast Asia, with the exception of Brunei Darussalam, Singapore, and – partially – Malaysia. Data is not available on the number of informal enterprises operating in the region, but – as a proxy – data collected on the rate of informal employment suggests a very high level of economic informality in the region (ILO). Informality appears to be most highly-concentrated in micro-enterprises that operate in low value-added services and unskilled labour-intensive manufacturing. Where it is pervasive, informality can slow skill and capital accumulation whilst constituting a source of unfair competition vis-a-vis more formal peers. The net result can be a slowing of medium-term economic growth whilst increasing inequalities between the employees of informal and formal enterprises. Policies to address this group of enterprises should consider that it is in an economy's interest to decrease informality over the long-term, but that such activities often provide livelihoods for many in emerging markets, and individuals are generally driven to create and seek employment in such enterprises out of necessity rather than opportunity.

3. SME policy as an economic and social development tool

SME policy is a tool commonly used by policymakers to promote economic and social development. Most countries have adopted explicit policies to support SME development and promote entrepreneurship, with the rationale that such enterprises make a significant contribution to employment generation. The argument follows that SMEs face pervasive market failures, such as structural under-investment in skills and technologies; higher transaction costs and wider information asymmetry gaps in dealing with financial institutions; and higher compliance costs, putting them at disadvantage relative to larger peers and increasing the probability that SMEs operate well below their optimal efficiency frontier.

The mainstream view is that public policy, if well designed and implemented, can address some of the most relevant market failures and generate a stream of social gains that are significantly larger than the direct cost of financing SME support programmes. Whilst there is general agreement on the overall logic underpinning SME development policies, such policies can adopt a number of different approaches. These approaches could also take into account other issues, such as sustainability (Box 4.1), or particular ways of collaboration with the private sector. These inform the type of policies that are selected and the structuring of such policies. They are as follows:

1. **SME policy as a tool to improve market efficiency.** This approach is broadly horizontal and laissez-faire. It aims to ensure that all enterprises have equal access to markets and factors, and to promote dynamic competition. It thereby focuses on removing the administrative barriers that may distort competition, reducing information asymmetries, promoting easy entry-exit procedures and stimulating entrepreneurship;
2. **SME policy as a structural challenge that requires targeted support.** This approach calls for a more proactive and ongoing policy intervention, direct support provided to enterprises until they have overcome most of their structural weaknesses. It places more emphasis on structural features that constrain SME growth – such as lack of economies of scales and scope, lower capacity to invest in human and physical capital, and weak R&D activity. It tends to target select groups of enterprises and sectors, which may change over time;
3. **SME policy as a tool to increase human welfare.** The main objective of this approach is to increase social development and generate additional employment opportunities. To achieve these aims, policymakers mostly focus on introducing schemes to support entrepreneurship, particularly amongst the most vulnerable, and to develop microfinance schemes and start-up support programmes. This approach mostly targets micro and small enterprises, mostly the former, and tends to focus on those operating in traditional, but highly labour-intensive sectors, such as hospitality, construction, transport, and small-scale manufacturing.

Policymakers very often adopt a mix of these different approaches, with the dominant approach fluctuating over time, in-line with current, often political, policy priorities. There is also a tendency across the OECD to adopt different approach for different segments of the SME population. This is also the case in Southeast Asia.

A number of instruments are available at OECD in order to analyse a range of SME policies at national level or at a regional level, comparing several countries or territories. Typically in order to analyse a set of SME related policies there is an *OECD SME Policy Review*. While for the analysis of the series of countries and benchmarking their performance there is an *SME Policy Index*. Please find out more about SME Policy Index Methodology in *Box 3.1*. This approach was applied for ASEAN in 2014 and in 2017-2018 (forthcoming, 2018) and further described in *Box 3.2* of the document.

Box 3.1. The SME Policy Index : Objectives and Methodology

The SME Policy Index (SME PI) is an analytical tool developed by the OECD, in co-operation with other international partners, to assess and compare progress in SME policies across economies and time. The SME PI was developed in the framework of regional programmes conducted by the OECD with partner countries.

The main objective of the SME PI methodology is to collect a wide range of information on policy inputs, harmonise this information and transform what are largely qualitative inputs into quantitative indexes that can be compared across economies and time. By regularly applying the SME PI over time, on average every three to four years, the participating economies are able to assess how their policies progressively align to internationally recognise good practices, respond to the needs of their SME population and converge towards a common set of goals and principles set at regional level.

All SME PI assessments share a common methodology. However, for each regional application, the methodology is adapted to respond to the specificities of participating economies in order to anchor the SME PI into the regional policy debate. The assessment is conducted through a questionnaire (the “assessment grid”) developed by the OECD jointly with the partner organisations and with experts and representatives from the participating economies and OECD countries. Each dimension includes one or more sub-dimensions, defined as a distinct area within a policy dimension (i.e. “Actions promoting financial literacy” within the dimension on “Access to Finance for SMEs”).

Each sub-dimension includes a number of indicators. Most of the indicators are qualitative in nature and aim at determining the key elements of the policy inputs. A number of indicators are quantitative, trying to measure the “intensity” of the policy actions. Assessment results are expressed in numerical indexes (scores) on a scale of one to five (one to six in the case of the ASEAN SME PI) and they are presented at the level of sub-dimensions and aggregated at policy dimension level. There is no single aggregate SME policy development score per country.

Please refer to Box 3.2 in order to relate to the process of the ASEAN SME Policy Index 2018.

Policy makers could also develop regular tracking tools for SME Policies such as SME Dashboard and SME Observatory which are applied in a number of countries and allow policy-makers have a more regular access to regularly updated information on SME population and crucial data.

Box 3.2. The ASEAN SME Policy Index 2018 as a way to benchmark SME Policies

The ASEAN SME Policy Index (ASPI) 2018 aims to provide a tool to identify the strengths and weaknesses that exist in the current SME policy and benchmark the status of implementation of the new ASEAN Strategic Action Plan for SME Development (2016-2025) to complement the ASEAN SME key performance indicators. The ASPI, scheduled for publication in 2018, is a joint effort between the Economic Research Institute for ASEAN and East-Asia (ERIA) and the Organisation for Economic Cooperation and Development (OECD). The development of the report and its methodology were formally acknowledged by the ASEAN Coordinating Committee on MSMEs (ACCMSME).

The ASPI is composed of sets of analytical indicators organised in dimensions. The assessment will be based on a comprehensive policy framework which allows for benchmarking not only among participating countries but also with international best practices. It targets to measure progress on policy convergence at the regional (ASEAN) level, improve SME policy-making in participating countries and enhance the capacity of policy-makers.

The eight dimensions of the Index are: Institutional Framework; Legislation, Regulation and Tax; Access to Finance; Access to Market and Internationalisation; Productivity, Technology and Innovation; Entrepreneurial Education and Skills; Green SMEs; and Social and Inclusive Entrepreneurship. By assigning scores to policy implementation level, the index attempts to convert qualitative information into quantitative results, facilitating cross-country comparison and allowing for systematic monitoring of policy developments.

The SME Policy Index is used in a participatory way with an approach consisting of complementary assessments conducted by the ASEAN countries themselves, through the National Co-ordinators, the Independent experts / Consultants, and by the OECD and ERIA. Over 400 people contributed to the development of the document, expected to be launched during 2018.

4. Three approaches to support inclusiveness through SME policy in ASEAN

The previous chapters suggest that inequalities are pervasive across ASEAN, and that these inequalities take a number of different forms. The following chapter will explore how three areas of SME policy can be used to tackle inequalities of income and opportunity across ASEAN, and the actions that are currently being taken in these areas by ASEAN policymakers. The three areas of SME policy have been developed for the purpose of this paper, and are as follows:

1. *Enhancing SME economic integration at the sub-national, regional and global level*
2. *Diffusing and supporting entrepreneurship through innovation policies*
3. *Enhancing economic opportunities amongst marginalised groups*

Approach 1: Enhancing SME economic integration at the sub-national, regional and global level

The prevailing economic growth model in the ASEAN region plays a strong emphasis on the integration into global value chains and on the development of export-oriented activities. Within this model FDI has given a central role in driving capital accumulation, technology transfer, upgrading of managerial techniques and access to foreign markets. This approach has worked well in the case of ASEAN-6 and it is still largely guiding economic development in the ASEAN-4.

There is however a growing understanding in the region that the base of economic growth has to be enlarged to include a vast network of local suppliers of services and goods, while retaining the GVCs integration and export oriented approach. In a number of cases this is necessary to diversify the production base beyond the current narrow sector specialization (this is the case for instance of Cambodia with a strong concentration in the garment sector), to root the presence of FDI by making foreign owned assemblers closely integrated with a network of local suppliers (as it is the case of the automotive sector in Thailand or the electronic sector in Malaysia), or to ensure the presence of local enterprises in technologically advanced sectors (as in case of Singapore and Malaysia).

Most AMS show strong trade growth during the last ten years. Indonesia, Thailand, the Philippines, and Malaysia experienced 8.1%, 6.1%, 4.8%, and 4% of average trade growth from 2006-2016, respectively. Less developed AMS experienced stronger trade growth in recent years with Cambodia, Lao PDR, and Myanmar had 13.6%, 14.1%, and 21.2% of average trade growth from 2011-2016, respectively. Thailand, Malaysia and Singapore also experienced large current account surplus.

Table 4.1. Trade data in AMS per country

	Current account balance (% GDP)	Average Exports to GDP 2014-2016 (%)	Average Imports to GDP 2014-2016 (%)
Brunei Darussalam	4.80	56.84	30.82
Cambodia	-8.60	61.77	26.59
Indonesia	-1.70	21.30	9.80
Lao P.D.R.	-9.60	37.00	13.70
Malaysia	2.40	70.69	36.54
Myanmar	-6.60	19.44	6.42
Philippines	-0.10	28.42	14.16
Singapore	19.60	181.17	100.3
Thailand	10.10	69.14	39.62
Viet Nam	1.30	89.94	45.62

Source: National statistics of AMS

Faster export led economic growth contributes to generate new and better jobs, as export-oriented enterprises are usually more productive than companies oriented towards local market and more likely to operate in a formal way. Export-led growth is also associated to economic diversification which broadens the productive base and generates more resources to finance human capital development through skill enhancement and better education, contributing therefore to more inclusive growth.

Public policy may support regional and global economic integration in several ways. Governments may interact directly at enterprise level, promoting linkages between large export oriented enterprises and small-sized local suppliers, i.e. by facilitating business matching, by supporting technological upgrading of local suppliers etc. Governments may also be engaged in direct export promotion, offering market intelligence services to SMEs, supporting the participation to trade fairs and commercial missions, helping local enterprises in navigating Free Trade Agreements and taking maximum benefits from the ASEAN economic integration process. In addition governments may take indirect actions, by promoting trade facilitation tools or and simplifying import-export procedures or by adhering to international standards, by signing mutual recognition agreements and helping enterprises in adopting internationally recognized technical and quality standards. Finally, connection with e-commerce platforms – national, regional or global – may open new opportunities for SMEs. Although e-commerce is dominated by private platforms, governments play an important role in defining the legal and contractual framework, in promoting the adoption of a secure on-line payment system, in facilitating cross-country e-commerce and in helping SMEs in adopting digital technologies.

Approach 2: Diffusing and supporting entrepreneurship through innovation policies

High-growth and innovative enterprises play a crucial role in fostering the development of a country enterprise sector, by ensuring that enterprise competition dynamic remains vibrant, by spurring productivity gains, by fostering technological upgrading and by generating new employment opportunities.

High-growth enterprises are defined by the OECD as enterprises that have recorded organic growth in terms employment or turnover of over 20% for at least three consecutive years and enterprise are engaged in the development. Innovative enterprises are instead enterprises engaged in the development of new products, new processes, in the discovery of new markets and in the introduction of new management techniques. A specific sub-category within the innovative enterprise typology is constituted by innovative start-ups, innovative enterprises less than two years old. Innovative start-ups have been at the front of current the digital and technological revolution. The most successful among them have been growing at exponential rate, becoming therefore the high-growth enterprises and they have contributed to define the new technological and productive frontier. In many cases they are taken over by larger technological groups, in a more limited number of cases they remain independent and sometimes achieve notoriety as unicorn, start-ups that are valued in excess of over one billion USD.

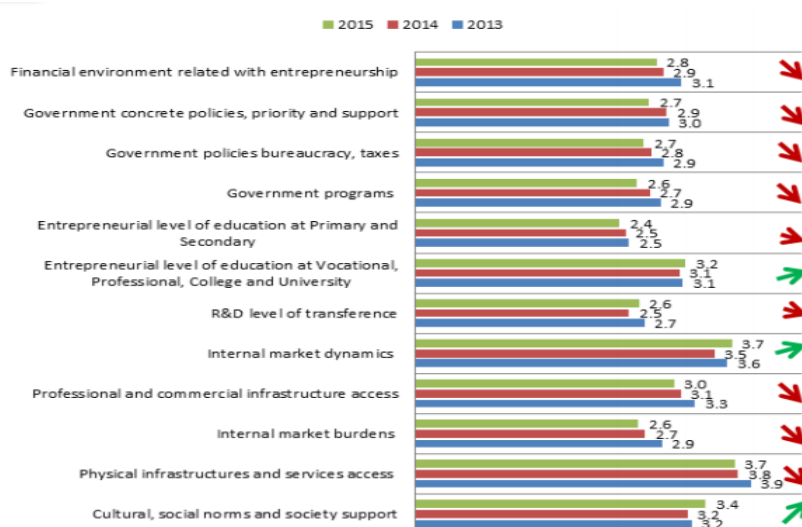
Several studies have highlighted the role of those types of enterprises. About 4% of all start-ups create over 50% of all new jobs in France. A 2011 World Economic Forum study reviews the growth path of HGEs across the world, finding that the top 1% of all companies ranked by the level of revenue growth contribute 44% of total sector revenue – with parallel findings for job creation. In the US, the study of the Kauffman Institute (2010) found that the top 5% of companies measured by employment growth created two thirds of new jobs, while the top 1% generated 40% of new jobs.

Governments often play an important role as coordinators, regulators and providers of basic research and early stage enterprise financing, but experience has shown that the government intervention has also clear limitations and cannot be a substitute for private sector players.

Innovative and high-growth enterprises may in the short term disrupt the activity of more established firms. This may have an impact on jobs and salaries for certain type of employees. As innovative and high-growth enterprise tend to concentrate in highly integrated hubs, their development may also increase geographic inequality within a country. But their contribution to economic growth, quality of living, widening of opportunities, is likely to compensate the negative impact on equality. Innovation if supported and complemented by policies that tend to re-balance the negative distributive effects and promote diffusion and participation, may be a force for greater inclusiveness.

The latest GEM reports on ASEAN (GEM, 2016) shows, framework conditions for high-growth entrepreneurs in ASEAN are relatively good, albeit in recent decline. The figure below shows experts perception of different aspects, graded on the Likert scale (the higher the score, the better). Aspects above average, potentially the source of future comparative advantage, include physical infrastructure and services, cultural and social norms, internal market dynamics, and perhaps, if the positive trend continues, entrepreneurial education.

Figure 4.1. Expert evaluation of ASEAN framework conditions for entrepreneurship



Source: GEM, 2016.

As with most indicators, this varies significantly from country to country – with Singapore, Malaysia, and Thailand scoring well, and Cambodia, Lao PDR, Myanmar towards the bottom of the rankings. The difference is more pronounced when looking at factor conditions relevant to the ICT-enabled activities a large portion of HGEs engage in. The World Economic Forum’s Networked Readiness Index finds that only Singapore, Malaysia, and Brunei Darussalam currently rank among the world’s top 50 countries for the quality of their digital environment and the extent of their technology usage. Lao PDR comes in at 104th place out of 139 economies; Cambodia – 109th; and Myanmar – 133d.

Approach 3: Enhancing economic opportunities amongst marginalised groups

Entrepreneurship promotion takes on a distinctly social approach in majority of AMS, and few countries, SME policy is predominantly used as a means to fulfil social policy objectives. Consequently, there are numerous examples of initiatives across the region to engage women, youth, and PWDs in entrepreneurship in response to labour market challenges, poverty alleviation objectives, to promote social inclusion and achieve gender equality.

In the region, AMS are consequently relying on a gender mainstreaming approach to women’s entrepreneurship development (OECD, 2017b). The Philippines is the only ASEAN country to have implementation formally fall under the lead SME agency, the Department of Trade and Industry. Women entrepreneurs in ASEAN have access to general SME support activities provided by governments, and the up-take of these services by women is relatively high in countries like Malaysia and Singapore.

Box 4.1. Promotion of Sustainability in ASEAN

Although not directly related to inequality, sustainable (green) growth is also important for reducing inequalities amongst current generations – research suggests that vulnerable populations are most at risk from climate change, particularly in the Asia-Pacific region, and that the impact of climate change is already being felt through extreme weather events and other phenomena.

Enterprise greening is an important element of sustainability strategies. SMEs, particularly those in the manufacturing sector, can be discouraged from greening their operations due to the high upfront costs often required to invest in new technologies. Greening SMEs could be an approach for AMS to promote innovation, and making SMEs from AMS become more competitive. By becoming greener and responding to the international environmental standards products of SMEs could be easier traded and could have easier access to the international global value chains.

Policymakers can utilise a wide range of tools to support enterprise greening. These include more targeted measures to support the development of green innovations and industries through instruments to enhance financial and/or market access, for instance, as well as horizontal measures to incentivise the greening of all enterprises, such as through regulatory incentives and eco-labelling initiatives. These measures would be listed in the Toolbox for Greening SMEs currently being developed by OECD for ASEAN.

Specifically for *youth*, many AMS recognised that youth entrepreneurship can be a policy tool to address issues of youth employment, social inclusion of disadvantaged youth, and informality within the labour market; and that in addition young people are capable of creating high-growth business ventures which may contribute to economic growth through innovation and job creation. Governments are also empowering and giving formal mandates to youth associations to carry out entrepreneurial activities.

Specifically on the *PWD*, nearly all AMS have laws and action plans to protect and enhance work and employment prospects for PWDs. Within ASEAN, Malaysia offers an array of support activities that range from start-up support, to export market access, to ICT training.

Conclusions: common and divergent themes

AMS have been going through a process of rapid change, economic growth and a number of structural challenges. Although many have been benefiting from the process of economic growth, the issue of poverty, income disparities and lack of support mechanisms for some marginalised groups is still an issue in some parts of ASEAN. Generally AMS often adopt an open policy-mix, combining elements from those three different approaches or adopting distinct approaches for each segment of the SME population with various levels of intensity. Each AMS has its own pace for integrating the issue of inclusiveness and has different issues they are focusing on.

AMS have also been catching up over the last years with the initiatives to tackle issues of productivity and innovation, and clearly these subjects have been high on the agenda of all of the AMS in the region. At the same time the region has achieved yet limited progress or uneven progress in the areas of promoting social entrepreneurship as well as entrepreneurship for marginalised groups. Similarly, few AMS have embarked on a strategic approach to promote SMEs greening. By further promoting all three areas affecting inclusivity, ASEAN could move ahead with the development of a more inclusive society and region.

Throughout the literature it has been noted that it is challenging to have access to comparable data across the region, and hence it is advised to promote comparison tools allowing policy-makers across the region to learn from each other and develop more efficient policies. Tools like ASEAN SME Policy Index could not only help policymakers gain a better understanding from the policies applied by their peers, but also have a better understanding of the current situation in each AMS through dedicated and more regular data collection efforts.

Reference

- DEPD (2014), *Brunei Darussalam Statistical Yearbook 2015*, Department of Economic Planning and Development, Bandar Seri Begawan, www.depd.gov.bn/DEPD%20Documents%20Library/DOS/BDSYB/BDSYB_2015.pdf.
- DeGain, C., B. Meng and Z. Wang (2017), “Recent trends in global trade and global value chains”, in *Global Value Chain Development Report 2017: Measuring and Analysing the Impact of GVCs on Economic Development*, World Bank, Washington DC, www.wto.org/english/res_e/booksp_e/gvcs_report_2017.pdf.
- GEM (2016), *ASEAN Regional Entrepreneurship Report 2015/16*, Universiti Tun Abdul Razak, Kuala Lumpur, www.unirazak.edu.my/images/about/ASEAN_Entrepreneurship_2015-2016.pdf.
- Kauffman Foundation (2010), “The Importance of Start-ups in Job Creation and Job Destruction”.
- OECD (2017a), *Economic Outlook for Southeast Asia, China and India 2017: Addressing Energy Challenges*, OECD Publishing, Paris, <http://dx.doi.org/10.1787/saeo-2017-en>.
- OECD (2017b), *Strengthening Women’s Entrepreneurship in ASEAN*, OECD Publishing, Paris, www.oecd.org/southeast-asia/regional-programme/Strengthening_Womens_Entrepreneurship_ASEAN.pdf.
- Lopez Gonzalez, J. (2016), "Using Foreign Factors to Enhance Domestic Export Performance: A Focus on Southeast Asia", *OECD Trade Policy Papers*, No. 191, OECD Publishing, Paris. <http://dx.doi.org/10.1787/5jlpq82v1jxw-en>.
- OECD (2015), “OECD Trade Facilitation Indicators: Moving ASEAN Forward”, OECD Publishing, Paris, www.oecd.org/trade/facilitation/oecd-tfi-asean-july-2015.pdf.
- OECD (2013), *Interconnected Economies: Benefiting from Global Value Chains*, OECD Publishing, Paris, <http://dx.doi.org/10.1787/9789264189560-en>.
- OECD and ERIA (forthcoming), *SME Policy Index 2018*, OECD Publishing, Paris.
- WEB (2011), *The Global Competitiveness Report 2011-2012*, World Economic Forum, Geneva, http://www3.weforum.org/docs/WEF_GCR_Report_2011-12.pdf.



ROLE OF SME POLICIES IN FOSTERING INCLUSIVENESS IN ASEAN

ASEAN SME POLICY INDEX AS A TOOL TO PROMOTE INCLUSIVENESS

ASEAN as a region has achieved remarkable progress on tackling the issue of inclusiveness through SME development over recent years. However, there are a number of challenges that SMEs still face across the region. These challenges are attributed to different factors including the changing landscape for international trade, a lack of resources to strengthen productivity, and the digitalisation and atomisation of manufacturing industries. This paper was specifically designed for policymakers from OECD and ASEAN, to provide the necessary background information on how SMEs policies could be used to promote inclusiveness. The ASEAN SME Policy Index 2018, currently being developed, could become a valuable tool for benchmarking relevant policies to further enhance inclusiveness. Its findings, once launched in 2018, could help policymakers to fill information gaps, and to have a better understanding of how their country's SME framework differs from that of their neighbours.

www.oecd.org/southeast-asia

www.eria.org

www.asean.org