

Strategies to Promote Small and Medium Enterprise in the New International Environment

By Amos Peters, Research Officer, ECCB

*I fear we shall outsleep the coming morn,
As much as we this night have overwatched
-Midsummer Night's Dream*

With the dawn of each new day, the challenges and implications of globalisation and liberalisation continue to unfold. Who would know better than the tiny Eastern Caribbean islands that stretch from Anguilla to Grenada? These micro-states continue, in compressed time, to make the transition from colonial status to a pampered form of independent status and in recent times to a neglected state.

In this new global village there are winners and losers, however the current trends in the global economy spell marginalisation for the small open economies of the Eastern Caribbean. Aid flows have dried up, concessionary financing has withered away and the preferential trade arrangements with the European Union are constantly under threat. These states have slipped from an annual average economic growth rate of 6 per cent per annum in the 1980's to a real growth rate of about 2 per cent during the 1990's.

These trends suggest that the OECS economies embark upon a path of strategic global repositioning. Global repositioning is a process whereby a country implements a strategic economic plan in order to improve its competitive position relative to other economies.

The new international environment refers to a world where the factors of production are free to move across regions and national borders, and markets are integrated. It follows therefore, that competitiveness is key to survival and consequently, the OECS economies need a strategic plan that ensures that they can compete globally.

The promotion of Small and Medium Enterprises (SMEs) is an efficient and effective strategy to reposition these small states and place them on a higher growth trajectory. Before outlining a few strategies to promote SMEs let us look at why they should be promoted.

In the United States SMEs employ about 50 per cent of the private work force, comprise more than half of the nation's Gross Domestic Product (GDP) and are the principle source of new jobs. In Poland it is estimated that SMEs contribute over 50 per cent of GDP and employ 60 per cent of the work force. Even in Russia where private sector activity was previously not encouraged, the share of SMEs in GDP is roughly 15 per cent and they account for about 13 per cent of the working population. In Kenya it was estimated that 12-14 per cent of the national income is generated by SMEs, and studies of 5 countries in Sub-Saharan Africa indicate that Micro and Small Enterprises (MSEs) employ 17-27 per cent of the adult population.

The aforementioned examples illustrate the importance of SMEs to employment and income of any nation. Outlined hereunder are some of the advantages of SME sector growth.

- (i) The private sector and more specifically SMEs form the backbone of a market economy and will provide the source of most new employment.
- (ii) SMEs play a substantial role in changing export patterns, thereby contributing significantly to the international competitiveness of the economy.
- (iii) SMEs are more people oriented, that is SME expansion implies that more people are directly involved in the economy as owners and have stakes in the performance thereof, and also in the stability of the society.
- (iv) SMEs facilitate innovation, technological change and research and development, which in turn make an economy more flexible.

A Look at Various Strategies

In an article of such limited parameters, it is impossible to detail and refine policy options, so instead the following outline of policy options, is presented hereunder.

First of all there must be a sound macroeconomic environment. This means low inflation, low unemployment, stable business cycles and a growing economy. Thus this creates business optimism and a stable planning environment, both of which fuel SME growth since as revenues and profits rise business owners become optimistic about the economy and their place in it.

Legislators should provide a positive legal environment with simplified tax and administrative procedures. For example, the registration period and licensing of new companies should be a short and easy process.

A low tax burden is critical to ensuring the birth and growth of SMEs. According to a survey by the National Federation of Independent Business in the United States, taxes were the main concern facing firms. This is not to say the same holds true in the Eastern Caribbean, but it is a major concern nonetheless.

Governments have a major role to play, through fiscal policy and institutional support. With regard to the former the governments of the region should cast their nets wider in order to attract Foreign Direct Investment (FDI) through services. Foreign investment enables a smooth transfer of 'best practice' to the region by way of a demonstration effect whereby Caribbean entrepreneurs can observe first hand the practices of foreign entrepreneurs.

Institutional support can and should be provided in two ways, namely financial and non-financial support. Since commercial banks usually have tough lending criteria, often requiring a business and credit history and since their lending is heavily collateral based as opposed to cash flow based, it is imperative that institutions such as the United States Small Business Administration (SBA) and the proposed Enterprise Development Fund (EDF), an ECCB initiative, are established. These institutions should be able to assess risk properly and provide venture capital for viable projects. These institutions would also back loans by private sector institutions. Under an umbrella the aforementioned policy options can be termed special incentive assistance programmes (provision of venture capital, credit guarantees, and small business loans). Other policy options such as tax credits and other incentives for start ups and/or increasing export production, implementing high technological innovations, environmental protection, and purchases of private entrepreneur inventory, may also be included under the umbrella term Special Incentive Assistance Programmes.

Under non-financial institutional support, come improving access to management, marketing, quality control, strategy and production and new technologies training. Advice such as tax advice and various forms of financial, technical and management assistance should be readily available to current and would be entrepreneurs to help start, run, and grow their business.

Finally, some other ways of expanding SMEs are to promote 'medium' sized SMEs as evidence shows that the small SMEs are inefficient, and tend to have a high failure rate. Moreover, enterprise development institutions should target already existing firms since trying to assist whoever comes through the door is a failing strategy. While providing incentives to SMEs, it is essential that in this increasingly competitive world, that governments do not coddle small firms but instead allow them to face realistic constraints. Both governments and enterprise development institutions should promote franchising, as franchises have lower failure rates relative to average start up failure rates. They already have systems in place and are generally easier to manage. Additionally banks and investors look more favourably on franchises. A system whereby SMEs engage in networking and sub-contracting should be encouraged since this creates economies of scale, increases survival possibilities and augments the economic linkages in the economy, both within and across and sectors and industries

In the final analysis the growth of SMEs in the region could be a component of a healthy and dynamic development process and should form the major part of an Eastern Caribbean development strategy.