

# Global Value Chain Development & SMEs' Participation



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## Global Value Chains & SMEs

Processes for production of goods and services have changed. It is not rare for a conception-to-commercialization process to cover multiple companies or multiple countries/territories. Coupled with the fast development of information and communication technologies that have allowed small and medium enterprises (SMEs) to easily get the same workflow tools as large corporations, global realignment of production processes and globalization of value chains create new business opportunities for SMEs. By participating in global value chains (GVCs), SMEs can enjoy the following benefits. First, they can improve the quality of technologies and human resources through increased opportunities for exposure, improved access to information, and introduction of new business methods. Furthermore, cooperation between the upstream and downstream sectors steps up improvement in SMEs' positions, promotion of information flows, and expansion of learning opportunities, boosting chances for SMEs to become successful in value chains. Successful SMEs in value chains can gain their independence from major companies and obtain further growth opportunities.

On the other hand, participation in GVCs can bring about not only business chances but also challenges in such aspects as management, funding, development of proprietary technologies and their protection, and innovation. For example, SMEs may face such problems as shortages in R&D funding, difficulties in human resource development, and tough requirements for product quality. They may also fail to secure sufficient operating funds when faced with payment arrears on the part of client companies. If SMEs are to improve their positions within GVCs, they must usually implement more massive and sophisticated operations. For example, SMEs will be required not only to manufacture products (or provide services) but also to develop products, organize and monitor sub-suppliers, implement internal quality management systems, reaffirm standard responses, provide products at competitive prices and secure good quality. Occasionally, SMEs' failure to recognize the complexity of problems may prevent them from participating in GVCs in a timely, effective manner. If SMEs are to be successful in GVCs, they have to address these challenges and cope with fierce global competition.

In view of such a background, a working party organized by the Organization for Economic Cooperation and Development (OECD) has undertaken research on "Enhancing the Role of SMEs in Global Value Chains" in cooperation with OECD and non-OECD countries and other international organizations. In the project, the Working Party on SMEs & Entrepreneurship, known as WPSME, looked into how SMEs' roles as large companies' traditional partners, suppliers and sales arms are changing on the globalization of value chains. The WPSME analyzed five industries (automobiles, scientific & precision

instruments, tourism, software, and film production & distribution) through case studies for specific industries or companies. In these five industries, the following value chain changes have been seen.

### Automotive Industry

While the automotive industry has undergone dramatic international realignments, each automaker has been aggressively promoting outsourcing at home and abroad in pursuit of greater efficiency. Original equipment manufacturing (OEM) deals, including open international procurements, have led to new pressures on SME suppliers in price negotiations and their price competition with low-wage countries, exerting a great impact on traditional value chains. Some SMEs with technological advantages have got out of automaker-led pyramid chains and become strategic partners of automakers. R&D and innovation are growing even more important.

### Scientific & Precision Instruments Industry

Sophisticated technological innovation capabilities, customization, response to rapid product obsolescence, and skilled labor linked to R&D are required for developing scientific and precision instruments. As many of such instruments are destined for niche markets, SMEs can make great contributions to value chains. But they face difficulties in securing skilled workers and protecting intellectual property rights. As markets are globalized, goods and services are increasingly combined into packages. In this sense, roles of global corporate giants have grown more important.

### Tourism Industry

Consumers, who used to be outside value chains for the tourism industry, have developed interactive relations with suppliers and intermediaries along with the spread of the Internet. As consumers have thus begun to play a key role in the value creation process, existing industry value chains have been changing dramatically. At the same time, globalization is making progress in the sector as major industry players are deepening relations with overseas SMEs through such means as franchising, management contracts, international reservation systems and brand development.

### Software Industry

This industry has faced rapid and fundamental changes in production and sales processes. It is one of the most globalized industries. SMEs have played as great a role as large companies in the industry, contributing to providing assistance tools and cycling ideas and concepts. The growing open-source movement is expected to bring about dramatic changes in traditional value chains led by big businesses, possibly affecting SMEs' positions and roles.

## Film Production & Distribution Industry

Complementary relations between content providers and distributors are very important in the film production & distribution industry. But their alliances, relative sizes and strategic strengths have changed dramatically on the introduction and diffusion of digital technology in the 1990s.

## Survey on Japanese Auto Industry's GVC

The following is an outline of the "Survey on the Japanese Automotive Industry's Global Value Chain" as implemented in 2006 by the Organization for Small and Medium Enterprises and Regional Innovation, Japan, known as SMRJ.

The yen's appreciation and intensifying trade disputes in the 1980s prompted Japanese automakers to step up a shift to overseas production. Now, their overseas production is almost equal to their domestic output. While automakers' expansion of production bases for finished vehicles means a wider market for parts suppliers, these suppliers are expected to choose primarily to build their production footholds close to automakers' assembly facilities. Reasons for the choice include (1) rising local content ratios stemming from such factors as production costs and host-country policies, (2) manufacture of products that accurately meet local market needs, and (3) strategic options with globalization in sight, including overseas production, increasing procurements from abroad and international division of labor. While automakers develop their global production systems, how to respond to these moves is strategically important for their SME parts suppliers (*see the chart*). The conditions for SMEs to take part in GVCs in the automotive industry are (1) accurate piece-processing technologies and satisfaction of purchasers' requirements for quality, delivery and cost, and (2) design and development capabilities. The second is an indispensable condition for SMEs' closer commitment to GVCs. In the survey, a poll was taken of domestic auto parts manufacturers, Japanese parts makers in Southeast Asia and automakers to find out structural characteristics of GVCs for the Japanese automotive industry. The poll found the following policy support guidelines.

- (1) SMEs in lower tiers get less information from value chains and have difficulties in providing products meeting trends and needs. In this respect, information infrastructure should be developed to allow them to collect accurate information.
- (2) Public-sector assistance may be offered to SMEs to help them improve their technological capabilities and upgrade their positions within value chains.
- (3) In order to promote innovations paving the way for SMEs to take part in value chains, support may be offered in the form of assistance for "industrial clusters" to enhance cooperation between regional universities/research institutes and SMEs.

## OECD Global Conference in Tokyo

The Ministry of Economy, Trade and Industry and the OECD will cosponsor the OECD Global Conference on "Enhancing the Role of SMEs in Global Value Chains" at Hotel Okura Tokyo on May 31 and June 1 this year. On the first day, Japanese and overseas businesspersons and researchers involved in the above-mentioned five industries will give presentations on

business models and research achievements while results of the survey of the five industries will be reported. On the second day, discussions will take place on the following four cross-industry subjects:

### (1) Innovation, R&D, Standards & Technology

Participants will discuss technology, R&D, and innovation for SMEs taking part in GVCs. Specific topics will include standards and certification, open procurement, platforms (including electronic platforms), international standard specifications, certification procedures, and development of information and communication technologies for promoting globalization of SMEs.

### (2) Intangible Assets & IPR Management

Discussions will focus on the management of intangible assets and intellectual property rights, including their optimum use, on the part of SMEs participating in GVCs. More specifically, participants will consider policy measures to assist SMEs in fighting against unfair business practices such as infringements of their IPR by their client companies and competitors.

### (3) Cooperation Mechanisms

Discussions will cover SMEs' cooperation (including industrial clusters, networks, and upstream/downstream cooperation) for successful achievements in GVCs. Cooperation between large companies and SMEs and problems attributable to the asymmetric power balance between them will be reviewed.

### (4) Conducive Global Business Environment

Conference participants will discuss development of a conducive global business environment including financing for SMEs' globalization. Participation in GVCs can bring about both greater business chances and new risks. Conference participants will consider policy support for developing a desirable business environment in a bid to promote cooperative relations between OECD and non-OECD countries.

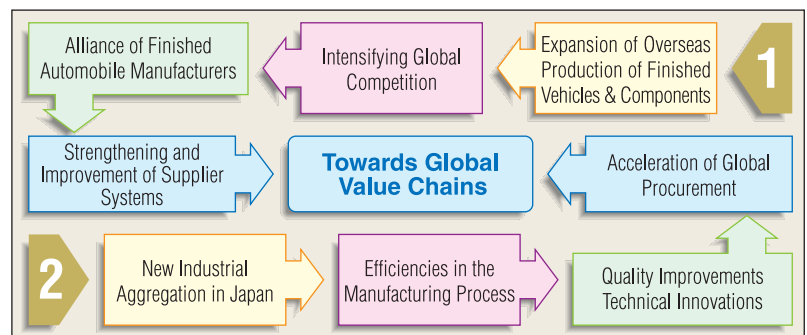
Based on discussions at industry-by-industry and policy-by-policy sessions, a "Tokyo Statement" will be published to spell out policy proposals for promoting SMEs' participation in GVCs and participating SMEs' development of their roles in such chains.

The conference will be held in two languages – Japanese and English – with simultaneous translation services provided. For more details, see the website for the conference at

[http://www.chusho.meti.go.jp/sme\\_english/conference/index.htm](http://www.chusho.meti.go.jp/sme_english/conference/index.htm).

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## Two Currents in the Creation of a Global Value Chain



Source: SMRJ