

SMEs: Their Current State of International Development and the Future Course of Policy Support

By Mochizuki Harufumi

Evaluation of SMEs' International Development

Small and medium-sized enterprises (SMEs) make up an extremely important part of the Japanese economy. For instance, they account for about 55% of total added value, 67% of all employees and 99.7% of the total number of companies.

With the rapid economic growth of China and other East Asian nations, Japan's large corporations have been advancing their global locationing strategies considerably since the 1990's. In this process, many SMEs are moving into East Asia alongside the large corporations in order to reduce the manu-

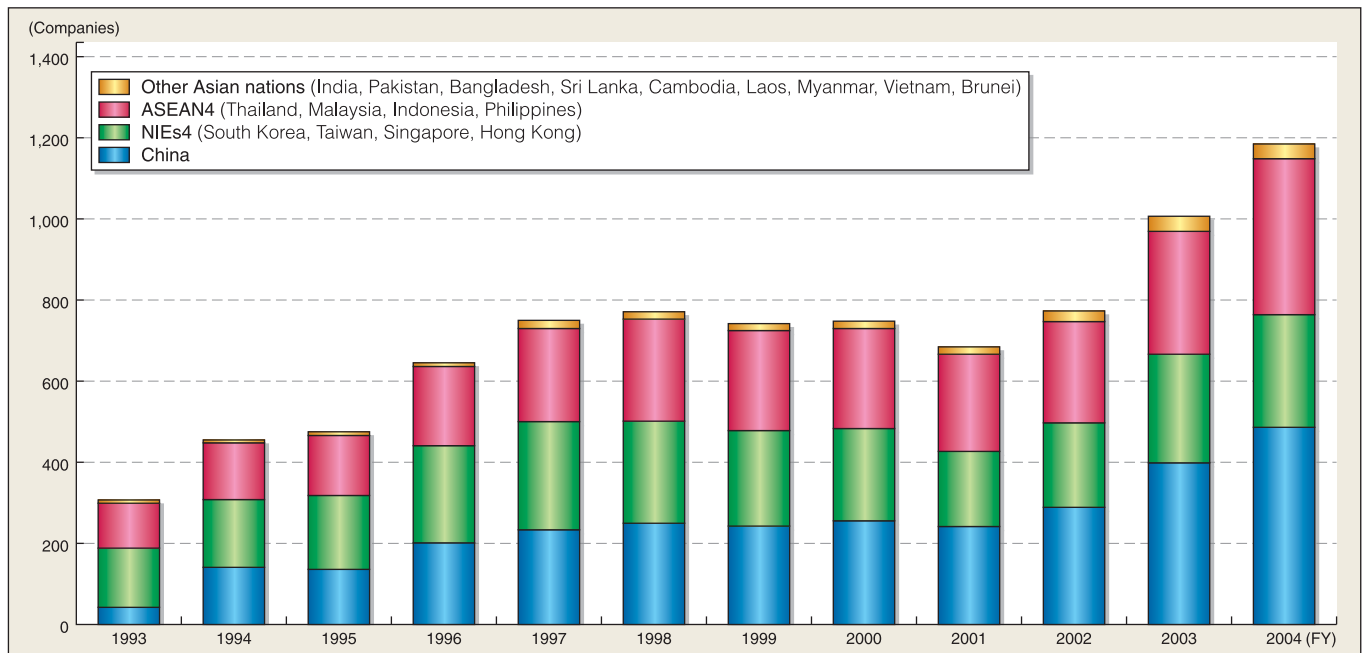
facturing cost of low-value-added products and to stay close to the large corporations from which they receive orders. For these SMEs, the advancing shift into East Asia is a survival strategy and with the dramatically changing business environment, many of them are aggressively pursuing international development to seek out new opportunities to develop and expand their business.

Figure 1 shows the numbers of locally-incorporated Japanese manufacturing SMEs in Asia. The 1990's saw an acceleration of moves into the East Asia region which actively accepts foreign capital development, to take advantage of the low-cost environment, particular-

ly personnel costs. While investment by Japanese companies in Asia was temporarily threatened by the 1997 Asian currency crisis, the Asian economies subsequently achieved a steady recovery, and Japanese investing activity continue to swell today. Advancing in China has surged to the extent that the phrase "overheat investment" has been heard over the past three or four years. As well as its high rate of economic growth in recent years, China's investment environment is improving, as evidenced by its 2001 accession to the World Trade Organization (WTO).

Taking an overall look at Japan's economy, such international development seems part of the necessary reform

Figure 1 Numbers of Locally-Incorporated Japanese SMEs Manufacturing in Asia



Source : Adapted from *Basic Survey on Overseas Business Activities*, Ministry of Economy, Trade and Industry, Japan

Note : SMEs are defined as those with capital of no more than ¥300 million provided by the head office corporation, or with no more than 300 full-time employees. For FY 1994 and 1995, however, SMEs were defined simply as companies with capital of no more than ¥300 million.

process to achieve an ideal international division of labor throughout the entire industry. With the growing borderlessness of economies and industries, companies are shifting their comparatively low-value-added processes, such as commodities, to East Asia where land prices and personnel costs are relatively cheap, while simultaneously maintaining and reinforcing the development and manufacturing of their high-value-added strategic products within Japan.

On the other hand, from the perspective of individual SMEs, international development helps to upgrade and make independent such areas as marketing, human resources, and production and development systems. Benefits like these have helped Japan's businesses overall, including its domestic businesses, to expand and become more sophisticated, and as a result, helped Japanese industry as a whole to achieve higher levels of added value.

Future Course of Policy Support for SMEs

Under such conditions, the government must promote the following two policies to strengthen Japan's SMEs in terms of global competitiveness.

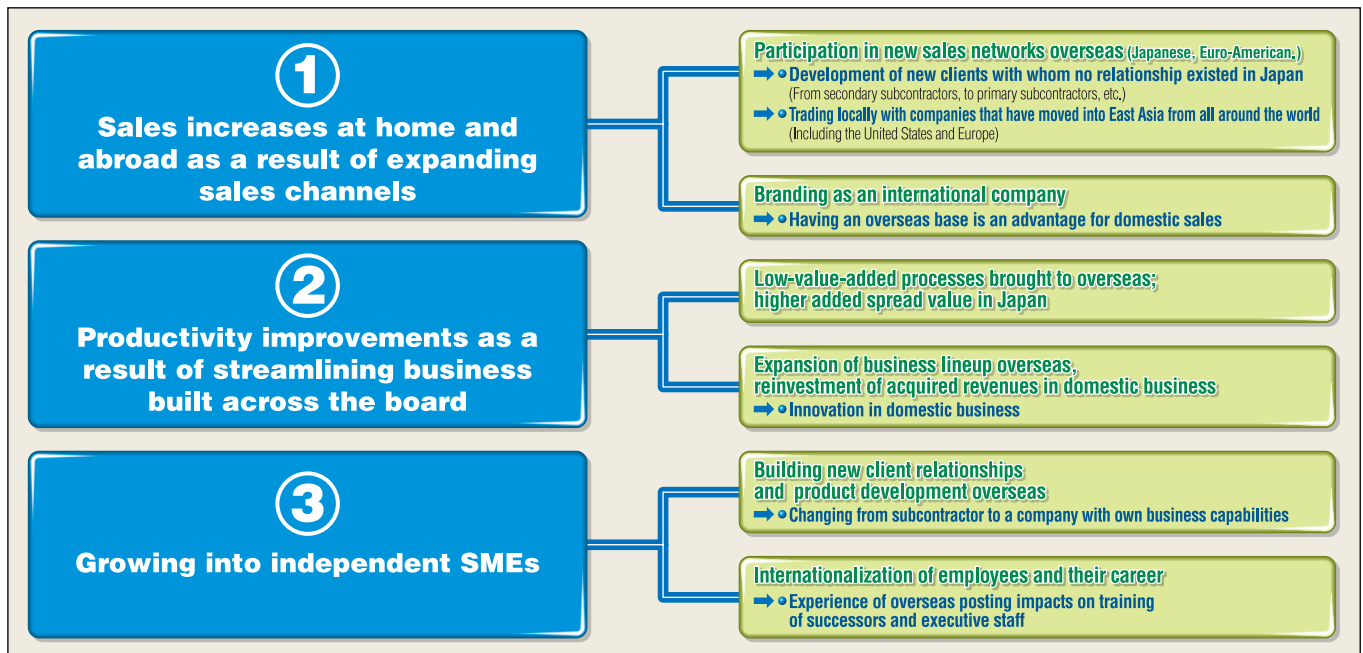
1. Reinforcing domestic infrastructure to further strengthen Japan's global competitiveness

The root of Japan's strength in the manufacturing industries is the strong ties "close fit" between groups of SMEs that possess the underlying technologies for *mono-zukuri* (goods production), such as molding, casting, plating, pressing and grinding, on the one hand, and the large corporations who supply the final products. The development of leading-edge strategic products is also a result of this "close fit" between.

In recent years, Japan's large corporations, having completed a round of moves into East Asia, are beginning to return to investment in Japan, with a focus on leading-edge industry areas, and an "investment boom" is occurring. One reason for this is a new appreciation of the domestic environment – the high technological abilities of the SMEs that provide the supporting industry within Japan. Therefore, it is necessary to strengthen the domestic foundations of the SMEs that supply the underlying *mono-zukuri* technologies in order to strengthen the global competitiveness of Japan's industry, as part and parcel of the above-mentioned reform process.

To achieve this, the Small and Medium Enterprise Agency submitted a bill, "Act to Promote the Enhancement of Manufacturing Technology for Small and Medium Enterprises" at the Diet on January 31, and plans to solidly promote

Figure 2 Examples of SME Business as a Whole Becoming More Sophisticated and Independent through International Development





the following overall policies.

Future vision of technology: Identify large corporations' needs in relation to underlying mono-zukuri technologies and develop a future perspective for the direction of the technical development that SMEs should aim toward.

Research and development: Offer prioritized support through funding, etc., for R&D projects undertaken jointly by SMEs.

Networks: Support the creation of "meeting venues" where SMEs can directly meet large corporations.

Human resource development: Support the training of technicians through technical colleges. Support the development of human resource programs through the academic industrial alliance.

Technology succession: Create a database of the industrial technologies and know-how accumulated by individual engineers and promote the efficient transfer of such knowledge.

2. Facilitate moves overseas and reduce risk

Next, while SMEs' international development is an essential reform process that will strengthen the industrial competitiveness of Japan as a whole, establishing an overseas presence involves many risks. When SMEs set up overseas, they face more difficulties than large corporations, lacking, for example, the capacity to gather the necessary information. Therefore, to facilitate the above reform process and to reduce the unexpected risks of SMEs relocating overseas, we intend to promote the following environment.

Provide information: 1) Advice on local laws, tax practices and labor. 2) Support feasibility studies for SMEs planning to set up overseas. 3) Dispatch survey missions to investigate the local investment environment.

Human resource securement: Support facilitation of securing local management-level human resources for SMEs.

Promote the improvement of local systems: Conduct survey on the state of unfair trading practices overseas, including the late collection of receivables and the counterfeit goods issue, and engage in policy dialogue with governments and other agencies of the countries concerned.

International Cooperation on SME Policy

Although they do not provide direct support for SMEs moving overseas, Japan's SME policies are regarded, in the eyes of the world, as very solid. In the area of intergovernmental cooperation too, Japan can point to many achievements to date.

Venues for SME policy cooperation are generally divided into bilateral forums, such as Economic Partnership Agreements (EPAs), and multilateral dialogues like the Organization for Economic Cooperation and Development (OECD).

Specifically, the international cooperation measures envisaged include building an SME business consulting system, disseminating simplified accounting standards for SMEs and supporting the establishment of public testing and research institutions and SME support institutions. These represent an attempt to transplant Japan's SME policies to East Asian nations, and should help strengthen the economic foundations of those countries and improve the local business environment for Japan's SMEs.

To achieve real, sustained revitalization of the Japanese economy, we must increase the vitality of SMEs in the mono-zukuri and other industries. The Small and Medium Enterprise Agency plans to continue flexibly promoting policies supporting the above structural changes, working in cooperation with related institutions.

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