CHAPTER 1

INTRODUCTION

This study attempts to learn about the role of government in promoting small and medium scale industries (SMIs) and its relations with the performance of SMIs in Malaysia. This study also attempts to raise awareness about the practices of governmental support policies and programmes to SMIs that form the backbone of our economy. Therefore, the question of promoting SMIs is important for both economic and political purposes.

For Malaysia, SMIs are important sources of employment, sources of goods and services for consumers, and are important suppliers for the large business sectors. Furthermore, SMIs use relatively few imported inputs and materials as compared to large business enterprises that are very much dependent on such imports. Therefore, the importance of SMIs must not be underestimated as it will continue to contribute to the growth and development of the economy.

Generally, there are various support policies and programmes including initial promotional activities, financial, training, technical support, infrastructure, consultancy services and marketing are undertaken by various agencies in assisting the establishment, growth and development of SMIs in Malaysia. However, there are many problems confronting the SMIs in Malaysia. All these include lack of capital for investment, limited and unequal access to institutional credit markets, under utilisation of capacity, inadequate infrastructure facilities, weak managerial and technical skills, labour shortage, rise in wages, violent exchange rate fluctuations, limited access to relevant business information, irregular access to domestic and imported inputs and materials coupled with high costs, inadequate access to information on foreign markets, lack of knowledge on governmental support programmes and policies, etc.

Besides all the problems faced by SMIs as stated above, there are also critics on the implementation of SMI programmes and policies in the country. Although the current 10-year policy (1991-2000, which falls under the National Development Policy) emphasises on qualitative rather than quantitative aspects of
SMI development, the ineffective co-ordination among the lead agencies that carry out the support programmes and policies, and many of them were merely duplicating the functions performed by each other only resulted in incremental growth of the SMIs. World Bank Report indicates that the level of technology and productivity of Malaysian SMIs are still low, not focused and thus not competitive. Furthermore, the network and linkages between the local SMIs and multi-national corporation have yet to be improved, with emphasis on the absorption and adoption of new, advanced and appropriate technologies. More relevant research and development institutions should be established in assisting productivity and quality of SMIs as well as the development of skilled human resource.

Malaysia is an open economy and subject to the vagaries of international trade, where international trade plays a very crucial role in the development and growth of our economy. Therefore, SMIs are facing globalisation of business. Hence, the government plays a very important role in assisting our SMIs to cope with circumstances such as dynamic competition in terms of increasing awareness of consumers and their demand for higher quality products at reasonable prices; rapid innovation and advancement in technology particularly in the field of microelectronics, material technology and biotechnology that require a shorter product life cycle; increasing competitiveness for investment especially with foreign investors; scarcity of financial resources; and also trading blocs such as North America Free Trade Area (NAFTA) and European Economic Community (EEC), that could both mean opportunities as well as threats, such as imposition of protective measures against our SMIs. The co-operation between leading government agencies and SMIs should be further reinforced to promote greater efficiency and productivity for SMIs, to ensure its competitiveness.


1.1 AREA OF STUDY

The promotion of SMIs have been an important strategy for the past 25 years with two main objectives namely redistribution of wealth and eradication of poverty. Thus, the role of government in promoting entrepreneurial growth has been perceived as very important. The role of entrepreneur has also been given much emphasis especially in developing our economy through technological transfer, innovation, employment, productivity and modernisation. Since independence, several institutions and agencies such as Majlis Amanah Rakyat (MARA), Bank Pembangunan Malaysia Berhad (BPMB), Malaysian Industrial Development Finance (MIDF), Malaysian Industrial Development Authority (MIDA), National Productivity Corporation (NPC), Ministry of International Trade and Industry (MITI) have been set up by the government to assist the development of SMIs.

SMIs have been singled out as a sector that receives and benefits from a diverse range of policy support and advisory assistance. Several incentives and facilities have been provided by the government to attract both foreign and local investments. All these include fiscal incentives, tax reduction, tariff protection, capital gains tax relief, infrastructure facilities such as free zones, industrial land and financial facilities that are available through a well-developed network of commercial or merchants banks and other financial institutions such as MIDF and BPMB. There are also advisory services and training provided by government agencies, such as MARA, SIRIM and Ministry of Human Resources. Under MARA, advisory services are provided by the Division of Advisory Services and Enterprise Development; while its training programmes arranged under the New Entrepreneurs Programme as well as under its Institute of Technology. The Ministry of Human Resources also provides training programmes especially through the National Vocational Training Council (MLVK) to establish and maintain a high standard of skill to meet the industrial demands.

It was noted that although technology is available to SMIs through various support schemes, the low level of managerial skills, technical knowledge and the relative weakness of support and training systems are major factors that collectively stunt the growth of SMIs, hence their contribution to the economy. Therefore, there is a need for a more integrated support programme to accelerate the capacity of SMIs to gain access to and better absorb the technology available.
1.2 PROBLEM STATEMENT

The SMIs are very important in contributing to Malaysia's economic growth and development. The importance of SMIs has been gaining recognition of the government with the formation of Ministry of Entrepreneur Development (MED) on 8 May 1995 with the main objective of developing entrepreneurs especially through its vendor development programme aimed at developing SMIs as reliable manufacturers and suppliers of industrial parts and components required by large industries and multi-national corporations.

However, there are various problems faced by the SMIs and the government has yet to draw up useful guidelines, implement programmes and policies to overcome some of the critical problems such as labour shortages, rising wages, limited access to institutional credit, limited access to acquire modern and appropriate technology, and subject to the vagaries of the world economy. Although the government has been well-aware of these problems and various institutions and agencies have been set up to promote the development of SMIs, there is still very little co-ordination among these institutions and agencies while many were merely duplicating the objectives and functions performed by each other. Thus, the adequacy, efficiency and effectiveness of such institutions and agencies in formulating governmental policies and programmes are still being debated and are subject to further testing. This has resulted in only incremental growth of our SMIs.

Since there is very little research being done in this area, there is not much feedback from the entrepreneurs on governmental policies and programmes. Therefore, the government is less informed and is faced with difficulties in obtaining useful information and comments on various support policies and programmes from the entrepreneurs. Furthermore, most SMIs also lack knowledge on governmental support policies and programmes. Some of them are even discouraged for the application of such support policies and services due to the amount of paperwork and time involved. Some of the entrepreneurs are also discouraged when their first application is being rejected, where they often perceive the processes involved are time consuming and ineffective. Therefore, the government should take appropriate steps such as giving more useful guidelines to the SMIs.
With the current population of 20 million, the domestic market is small and our SMIs have to penetrate into the bigger regional and international market. However, our SMIs have been greatly relying upon imported technologies and machinery from developed countries that are very costly for their production purposes. This inevitably causes an increase in the cost of production leading to the decrease in value-added, thus making the products of our SMIs less competitive in both regional and international market. Therefore, the government has yet to ensure the maintenance of our SMIs' competitive edge in the international market. Although various education, training, research and development programmes, and advisory services are being intensified to increase our SMIs' competency, efficiency and productivity, many of our SMIs have yet to achieve optimisation capacity.

Realising the various problems as stated above, the government feels that it is a need to promote and accelerate the development of SMIs, particularly in the manufacturing sector, through the establishment of a single agency. Therefore, Small and Medium Scale Industries Development Corporation (SMIDEC) was established on 2 November 1995, and is officially in operation on 1 May 1996.

The primary objective of SMIDEC is to promote and accelerate the development of SMIs, with other objectives which include to increase the value-added contribution of the SMIs to manufacturing output; to nurture and enhance the entrepreneurial skills of the SMIs; and to increase the capacity for technological absorption and advancement in the technological capability of the SMIs. Some of the functions of this corporation include being the centre for collection, reference and dissemination of information related to SMIs; to promote mutual co-operation among SMIs through amalgamation of businesses, technical co-operation, establishment of mutual fund or co-operative enterprise and the procurement of common equipment; to encourage industrial linkages with large industries and many others.

The establishment of SMIDEC is hoped to reduce the inefficiency and ineffective co-ordination among various agencies that formulate support policies and programmes. It is also hoped that this corporation would enable a comprehensive planning of the SMI programmes and activities, at the same time improve the co-ordination and networking with other institutions and agencies involved in the promotion of SMIs to reduce duplication of objectives and functions. It is further
hoped that this corporation would nurture our SMIs into home grown MNCs, in line with the Malaysian industrialisation process and Vision 2020. However, this corporation is still at its infant stage and time is needed to proof its capabilities in achieving its goals and objectives.

1.3 OBJECTIVES OF THE STUDY
The primary objectives of this research are:

1. To identify the types of governmental support in terms of its specific functions which include incentives for investment, financial support, governmental non-financial and technical support (such as infrastructure, industrial sites, research and development, etc.), supply and marketing support, in addition to training and advisory services;
2. to focus on the adequacy of types of governmental support in promoting SMIs;
3. to analyse the profile of SMIs;
4. to identify problems faced by entrepreneurs;
5. to recommend some guidelines to overcome problems faced by SMIs in getting the governmental support; and
6. to recommend some guidelines from public administration point of view to assist in formulating policies in the future.

1.4 SIGNIFICANCE OF THE STUDY
A questionnaire is developed to obtain information on the profile of SMIs and the extent to which they have benefited from the policies and programmes. Since SMIs play a very significant role in our economy, it is important to analyse and evaluate the adequacy of governmental support policies and programmes in promoting them and at the same time contribute toward national interest.

Furthermore, this study is timely as has been done so far on evaluating the role of government in promoting SMIs. It is hoped that this study will highlight the weaknesses of government support policies and programmes to enable future improvement.

As there have been only a few studies on SMIs especially in Malaysia, it is hoped that this study will be able to add to more resources on this field. It is also
hoped that this research will help to instigate more interest among researchers to carry out further research in this area, especially on rural industries.

The significance of this study can also be shown as the government is giving more emphasis to develop rural areas, at the same time provide more employment opportunity and sources of supplementary earnings to rural areas as a way to curb income inequality. There are various special incentives given to companies located in Sabah, Sarawak and the designated "Eastern Corridors" of Peninsular Malaysia that covers Kelantan, Terengganu, Pahang excluding the districts of Lipis, Raub, Jerantut and Cameron Highlands (except for approved industrial estates located in these districts) and the district of Mersing in Johor.

1.5 SCOPE OF STUDY

The study is restricted to SMIs in the State of Selangor and Federal Territory. It covered only the manufacturing sector, ranging from simple food production to capital intensive chemical and auto parts industries. However, not all SMIs in these areas were covered in this study, but a sample size of 296 companies/enterprises were chosen randomly based on records from the Registrar of Companies, Ministry of International Trade and Industry, MED, Persatuan Pengilang-pengilang Bumiputera Malaysia, as well as Federation of Malaysian Manufacturers. The study only evaluates the entrepreneurial development policies and programmes based on the SMIs' point of view.

In this view, performance of SMIs is evaluated based on paid-up capital as at 31 December 1995, and also profit ability of firms. According to Ministry of International Trade and Industry (MITI), the definition of SMI is based upon the amount of shareholders' funds not exceeding RM2.5 million or not exceeding 100 employees. However, this study is based upon the definition of paid-up capital not exceeding RM500,000 or not exceeding 20 employees for small scale industries, while paid-up capital between RM500,001 to RM2.5 million or number of employees between 21 to 100 for medium scale industries. This enables the inclusion of small and medium scale industries in this study.
1.6 RESEARCH FRAMEWORK

The definition for SMIs is based on the Small Enterprise Division of MITI, where a small scale industry is defined as one with paid-up capital of up to RM500,000 or having less than or equals to 20 full-time employees; a medium scale industry as one with paid up capital of between RM500,001 to RM2.5 million or having between 21 to 100 full-time employees. Therefore, only 67 firms are analysed in this study, comprising of 45 small scale industries (67.2 percent) and 22 medium scale industries (32.8 percent).

Results of the characteristics of the firms is shown in Table 1.1. It shows the number of employees by paid-up capital of the firms. This research categorises firms with paid-up capital of RM500,000 and below as small scale industries, while firm with a paid up capital of between RM500,001 to RM2.5 million as medium scale industries. However, two firms with paid-up capital of more than RM2.5 million, but had less than 100 employees will also be categorised for simplicity as medium scale industries. Only one firm with paid-up capital of more than RM2.5 million and has more than 100 employees is thus excluded because it is deemed large firm, and is therefore out of the scope of this research.

Table 1.1: Number of Employees by Paid-up Capital

<table>
<thead>
<tr>
<th>No. of employees</th>
<th>≤ RM500,000</th>
<th>RM500,001 - RM2.5 million</th>
<th>&gt; RM2.5 million</th>
</tr>
</thead>
<tbody>
<tr>
<td>≤ 20 employees</td>
<td>25 (36.8)</td>
<td>2 (2.9)</td>
<td>-</td>
</tr>
<tr>
<td>21 - 100 employees</td>
<td>18 (26.5)</td>
<td>15 (22.1)</td>
<td>2 (2.9)</td>
</tr>
<tr>
<td>&gt; 100 employees</td>
<td>2 (2.9)</td>
<td>3 (4.4)</td>
<td>1 (1.5)</td>
</tr>
<tr>
<td>Total</td>
<td>45 (66.2)</td>
<td>20 (29.4)</td>
<td>3 (4.4)</td>
</tr>
</tbody>
</table>

Shaded area denotes medium scale industries.
Figures in parentheses denote percentages.
Source: Survey.

1.7 MODEL

There are various approaches adopted by the government to promote SMIs. Some approaches are partial, such as providing specific incentives for investment, financial assistance, technical training, infrastructure facilities or consultancy services. However, the model used in this study as illustrated in Figure 1.1 shows a comprehensive and integrated approach (a combination of all three approaches) in the promotion of SMIs for the entire community.
The figure illustrates the government and private sector intervention, through various institutions and agencies in formulating and implementing support policies and programmes in order to promote SMIs. The model touches on types of governmental support policies and programmes, and three broad approaches to promote and develop SMIs. Realising that SMIs are faced with various problems, various support policies have been implemented to develop SMIs as supporting industries to heavy industries and other business entities. Various types of governmental support policies and programmes include initial governmental promotional activities; financial support; government non-financial and technical support (such as infrastructures, industrial areas, research and development, etc.); supply and marketing support; and training and advisory services.

The three broad approaches to entrepreneurship development include:
1) changing the environment: focus on laws and regulations, fiscal incentives and infrastructure facilities;
2) training and consultancy programmes: improving entrepreneurial, managerial and business competence;
3) promoting entrepreneurial culture: programmes to make specific communities more entrepreneurially oriented.

Figure 1.1: Promotion of Small and Medium Scale Industries

Source: Constructed from analysis of related literature.
All three approaches as stated above were undertaken by various government agencies and institutions in promoting and developing SMIs. Recently, SMIDEC was established to provide a national administrative focus point on SMIs and at the same time provide an effective and efficient institutional mechanism in channelling all the necessary support services to SMIs to ensure an integration of all the three broad approaches. The links between the government and SMIs represent the transfer of resources including skilled manpower, ideas, institutional support and finances. The link between the support policies and programmes, and small and medium sized enterprises are vital for the latter to succeed.

1.8 HYPOTHESES

Several hypotheses can be formulated from the model depicted in Figure 1.1. The main hypotheses are as follow:-

Hypothesis One: There is a significant association between size of firms and utilisation of incentives and facilities.

This hypothesis includes the following sub-hypotheses:-

a. There is a significant association between size of firms and utilisation of incentives for investment.
b. There is a significant association between size of firms and utilisation of financial and credit facilities.
c. There is a significant association between size of firms and utilisation of marketing programmes and facilities.
d. There is a significant association between size of firms and utilisation of infrastructure facilities.
e. There is a significant association between size of firms and utilisation of training programmes and advisory services.

Hypothesis Two: There is a significant association between size of firms and various problems faced by entrepreneurs.

This hypothesis constitutes the following sub-hypotheses:-
a. There is a significant association between size of firms and human resources/managerial problems faced by entrepreneurs.
b. There is a significant association between size of firms and financial problems faced by entrepreneurs.

c. There is a significant association between size of firms and marketing problems faced by entrepreneurs.

d. There is a significant association between size of firms and governmental problems faced by entrepreneurs.

e. There is a significant association between size of firms and production problems faced by entrepreneurs.

f. There is a significant association between size of firms and raw material problems faced by entrepreneurs.

g. There is a significant association between size of firms and other problems faced by entrepreneurs.

Hypothesis Three: There is a significant association between size of firms and market coverage of the SMIs.

Hypothesis Four: There is a significant association between size of firms and turnover of the SMIs.

Hypothesis Five: There is a significant difference in profit ability between small and medium scale industries.

Hypothesis Six: There is a significant association between year of commencement and utilisation of incentives and facilities.

The above hypothesis constitutes the following sub-hypotheses:-

a. There is a significant association between year of commencement and utilisation of incentives for investment.

b. There is a significant association between year of commencement and utilisation of financial and credit facilities.

c. There is a significant association between year of commencement and utilisation of marketing programmes and facilities.

d. There is a significant association between year of commencement and utilisation of infrastructure facilities.
e. There is a significant association between year of commencement and utilisation of training programmes and advisory services.

1.9 RESEARCH METHODOLOGY

Studies on entrepreneurship involve specific group of people, particular methodologies and specific objectives. There are a few steps taken to obtain data for this study:

1.9.1 Primary Data

There is no single agency that govern SMI. Hence, information on each SMI needed to be obtained from a few parties. First of all, addresses of the respondents were gathered from the Ministry of International Trade and Industry (MITI), MED, Registrar of Companies, Persatuan Pengilang-pengilang Bumiputera Malaysia, as well as the Federation of Malaysian Manufacturers. A total of 421 addresses of the SMIs were obtained from these organisations, and 296 respondents (about 70 percent) were selected in this research by using a simple random sampling method. The questionnaires were then mailed to all the respondents with self-addressed, stamped return envelopes. Telephone calls were made to almost 80 percent of the respondents after one week of mailing of the questionnaires. On the second week, telephone calls were made to companies that stated they did not receive the questionnaire mailed to them. Follow-up questionnaires were send to almost 20 percent the respondents who did not receive them. Due to inadequate number of response, interview survey was carried out on the fourth week. The respondents were assured that this research is purely of academic interest only, and they could obtain information on various incentives and facilities offered. Some of the respondents were even assured that they can obtain a summary copy of this research as a way to convince them to answer the questionnaire. The whole primary data collection procedure took about two months.

In this study, both self-administered questionnaire and interview survey were chosen for practical reasons. Self-administered questionnaire was chosen due to budget and time constraints. At first, a mini pilot survey was conducted on three SMIs by interview. The questionnaire was then revised based on the results of the mini pilot survey to further improve it. The questionnaire consisted both Bahasa
Malaysia and English versions. The questionnaire was divided into four parts (see Appendix A).

Part A of the questionnaire is geared to obtain company profile. In Part B, the researcher obtains information on the awareness and utilisation of various incentives and facilities by SMIs. Part C of the questionnaire is also important because it helps the researcher to identify various problems faced by SMIs. Part D further helps the researcher in getting general perception of the SMIs on various programmes and facilities as well as their comments on ways of assistance, programmes and advisory services that can improve their business performance.

Another method of data collection is through interview surveys. In such surveys, both structured and unstructured interviews were carried out in this study. Unstructured interviews were used mainly to obtain more in-depth information on certain selected questions and at the same time to identify some critical problems faced by entrepreneurs. The respondents were guaranteed that all individual information obtained will be treated with strict confidence, and that the objective of this research is only to evaluate the entrepreneurial development policies and programmes based on the SMIs’ point of view.

1.9.2 Secondary Data

The study uses a collection of a number of published material relating to the agencies assisting SMIs. The purpose of this method is to gather the agencies' objectives and their role in promoting SMIs. The main objective is to evaluate the adequacy and effectiveness of the policies and programmes. The purpose of this study is not to evaluate the performance of the agencies involved, but to have a better understanding and information on the support programmes available to SMIs. Some of the information on support programmes and incentives are gathered from MITI's and MED's homepage through internet. This study also uses annual reports, such as reports from MITI and Bank Negara Malaysia. Governmental and policy documents were also used in this study. Besides that, this research also refers to various books, journals and theses available.
1.10 LIMITATIONS OF THE STUDY

This research only covers SMIs in the Klang Valley, and 12 main business activities by SMIs. The number of companies covered is very much governed by time and budget constraints. Data are collected based on both interview and self-administered questionnaire survey, thus may be subject to biases. This research managed to get 72 respondents out of 296 questionnaire distributed by mail, yielding a response rate of only 24.3 percent. Furthermore, not all the questionnaire returned were fully answered. The researcher managed to call up some of the companies that did not fully answered their questionnaire. The remaining four questionnaire have to be discarded because the researcher was unable to contact them. Only 68 questionnaire were usable for this research.

The researcher faced difficulties in getting cooperation from the respondents. Although the researcher had managed to contact almost 80 percent of respondents by telephone calls after mailing the questionnaire, 224 of them still did not reply. Despite being assured that this research is purely of academic interest only, many of the respondents were reluctant to disclose information about their businesses.

1.11 ORGANISATION OF CHAPTERS

This study is divided into six chapters. Chapter 2 focuses on literature review on entrepreneurial theories and SMIs while Chapter 3 describes lead agencies as well as various policies that are assisting SMIs. Chapter 4 analyses on profile of SMIs, various programmes and incentives provided for the development of SMIs, as well as the extent of various problems faced by SMIs in the Klang Valley. Chapter 5 presents further analyses as well as hypothesis testing, while Chapter 6 ends the study with summary of findings, conclusions and recommendations.