Small Business and International Competition

—Strengthening the International Competitiveness of Small Business—

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I. The World Economy of Today

For the past 30 years, the world became more interdependent through trade, capital, and migration. These links affect all nations by spreading economic problems from country to country as they provide benefits for nations around the world. This phenomenon can be illustrated more vividly by the recent World Bank Development Report. This report described that large fiscal deficits, tight monetary policies and concerns about inflation in the industrial countries have raised real interest rates to unprecedented levels, curtailed growth and depressed export earnings of developing countries. With their abiltiy to buy imports and service, their debt thus reduced, many developing countries have had little alternative in the short term but to reduce growth.

Furthermore, development prospects for the international economy have worsened over the past years. The report lists reasons for pessimism; continuing recession in the industrial countries (which also heightens the threat of protectionist measures), the developing countries' adverse terms of trade and depressed export volumes, high and more volatile interest rate that limits

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borrowing, and large debt repayment burdens.[1]

Under the present conditions of world economy, the developed countries will suffer from the sluggish growth and the developing countries will suffer from decline in commodity prices, poor prospects for commercial borrowing, and deteriorating opportunities for export.

II. Foreign Trade as a Global Challenge

Since the economic aftermath of the 1973 oil embargo and the consequent energy crisis, foreign trade as a means of international business has become significantly more critical to a nation than other means such as licensing, joint ventures, and local production through foreign investment. Faced with sharply increased prices for the imports of fuel and manufactured goods, most of nations, especially the developing countries, have to boast their exports to balance their payment of foreign exchange.

The primary reason for the rise of foreign trade may be traced to the salient features of export and import activities by a company. That is, foreign trade provides several advantages for a company over other methods of international business and simultaneously satisfies both national and corporate objectives.

The first and probably the biggest factor of foreign trade is that it is not only a necessity for a country but also it is good for the survival and ensured growth of the company. In any cases, foreign trade is within the reach of every company, big or small, and there are virtually no scale factor to start with. Also foreign trade activities require less financial and managerial resource commitments than other methods of international business.

The second reason for the rise of foreign trade can be traced back to the small size of the domestic market.

(1) "World Bank Development Report," *The Asian Wall Street Journal*, Dow Jones Company, Inc., August 17th, 1982.

This factor has been a major reason for developing countries which usually have so small local markets. However, foreign trade is also increasingly recognized as an equally important factor for small companies in developed countries. The primary reason is the fact that most products for small companies tend to have a high degree of skewed consumption which leads to the popular market heuristic of 20/80 ratio: 20 percent of customers generate 80 percent of total business revenue for a product category.(2) When additional sales are generated by exports, a company can lower unit cost at higher volumes since the same manufacturing facility is utilized to greater volume of production, which will provide the company with advantages over competiton. This kind of competitive edge cannot be obtained at all or to the same extent when a campany is engaged in other forms of international business such as licensing, joint ventures, or foreign investment. Thus, some research asserted that the German and Japanese companies have significantly achieved the competitive edges over the U.S. companies mostly because they have remained export-oriented whereas the U.S. companies have leaned heavily in the past toward private foreign investment as a way of doing business internaionally.(3)

The third factor that contributes to the rise of foreign trade is the economic incentives and other official measures offered by the government. Many governments use a variety of measures to encourage and facilitate foreign trade, especially exporting. These measures can be classified into four categories:

1. Tax incentives; including tax credits and rebates, and other direct and indirect tax preferences within the tax structure.

2. Financing and insurance; including all exports credits, export insurance, insurance guarantees.

3. Information and promotion; including information services to foreign

(2) Jagdish N. Sheth, "Emerging Importance of Export Marketing for U.S. Products," Jagdish N. Sheth et al. ed., *Export Marketing: Lessons from Europe*, Bureau of Economic and Business Research, College of Commerce and Business Administration, University of Illinois, Champaign, Illinois, July, 1980, p. 6.

(3) *Ibid.*, p. 4.

traders, and other promotional activities.

4. Other official measures; such as incentives in terms of import licenses and so forth.

These incentives often lead for companies to sell their products at or below cost, resulting in a fierce competition in the foreign trade. In many instances, the economic incentives for export are often strong enough to encourage companies to sell their products at or below cost in the oversea market and to charge excessively higher margin in the domestic market to cover the loss stemming from the below-cost export. The degree to which such double pricing system practices depends on the extent of export incentives and the elasticity of demand for the product.

In summary, foreign trade provides the means for a country as well as a company to sell goods and services for which it has a comparative advantages and to import goods and services it needs. In this scheme of foreign trade, exports become more important part because they provide an expanded market and at the same time generate foreign currency needed to pay for imports. Since one country has to balance the payment of foreign exchange to maintain economic stability, national governments adopt a variety of measures to promote export of their country. Thus, it increases the competition in the foreign trade and results in fierce competition for export.

The amount and intensity of government export promotion varies greatly, as shown by the following Table-1[4]

Table 1. Amount and intensity of government export promotion

Country	Value of 1976 exports (in US $ billions)	Government export promotion spending (in US $ millions)	Relative promotional intensity spending (per $ 1,000 of exports)	Percent of exports supported by government credits or guarantees
France	$ 56.6	$ 80.7	$ 1.43	30
Japan	67.7	60.7	.90	42
W. Germany	103.6	15.5	.15	12
U.K.	46.0	95.7	2.08	34
U.S.	114.9	64.7	.56	7

However, regardless of these measures, it has been demonstrated time and again in all countries with major exports that successful exporting ultimately depends on the initiative, drive, and entrepreneurial ability of individual companies.[5]

III. Problems in Foreign Trade of Small Companies

Despite these developments which have created opportunities in international business for sales and profits, most small firms, particularly the manufacturing firms, fail in taking advantage of the available opportunities. It is noteworthy that the smaller a company is, the less a company is engaged in export, as evidenced by the following Table-2.

Table 2. Sales by market for small business in Korea

Number of employees	Domestic market	Oversea market(%)
5∼ 9 persons	98.9	1.2
10∼ 19	89.5	10.5
20∼ 49	77.1	22.9
50∼ 99	75.8	24.2
100∼199	73.2	26.8
200∼299	68.9	31.1

Source: Survey of Small Business, Ministry of Commerce and Industry, Republic of Korea, 1980.

For small business which hires less than 50 persons, they sell 77% or more of their products to domestic market, and only 22% or less of their sales come from the oversea market. In contrast, small business which hires 200∼299 persons obtains one third of business from oversea market. In the Table-2, it is interesting to notice that as the size of company gets larger in terms of employee number, the proportion of oversea market steadily increases.

One reason for this failure may be due to the fact that many companies perceive their small size as a constraint. Some firms believe that they cannot

(4) Congressional Research Service, Library of Congress, Export Stimulation Programs in the Major Industrial Countries: The United States and Eight Major Competitors, U.S. Government Printing Office, Washington, D.C., 1978, p. 18.

(5) L.A. Walker and Hanns-Martin Schoenfeld, "The Role of Government in Promoting Exports: A Survey of Official Measures in Five Major Countries", Jagdish N. Sheth et al., *op. cit.*, p. 65.

compete in international markets successfully because of certain problems and limitations related to small size. Table-3 shows major management problems perceived by small business in Korea. According to Table-3, small firms with less than 50 employees indicate that their utmost problem is the lack of sales, while small firms with more than 50 employees perceive the rise in raw material cost and wage as the utmost management problem.

Table 3. Major management problems for small business(%)

Number of employees	Rise in raw material cost	Rise in wage	Lack of sales	Lack of capital	Low level of technique	Insufficient production facilities	Difficulties to obtain skilled workers	Others
less than 50	32.3	10.9	34.9	14.9	1.6	3.5	2.2	0.6
50～ 99	39.9	7.1	28.2	12.4	2.0	2.4	6.8	1.3
100～199	43.2	8.9	20.9	15.0	0.3	3.7	6.2	1.8
200～299	39.1	13.4	20.4	16.7	1.6	2.4	4.6	1.8

Source: Survey of Small Business, Ministry of Commerce and Industry, Republic of Korea, 1980.

In general, as the size of companies is smaller, the lack of sales becomes a very serious problem. For smaller firms, it is difficult to get involved with foreign market in addition to domestic market due to limited manpower, product lines, production capacity and capital. Most of smaller firms prefer to deal with domestic market as the following Table-4 shows.

According to Table-4 only 1% of small firms with less than 9 employees are involved with export business and 98% of them even do not have any plan to get involved with export in the near future (within 3 years). Small firms with 10～19 employees show similar entrepreneur attitude, i.e., only 10% of them are either involved with export business, while 90% of them have no plan to develop involvement in foreign market. The statistics change drastically as the size of firms gets larger. In the Table-4, small businesses with 200～299 employees show that 68% of them are already in export business and furthermore about 10% of them have plan to develop export business. Only 23% of them do not have any plan to develop involvement with export market in near future.

Table 4. Number of companies in export business (%)

Number of employees	Sample size	Already in export business	Plan to export within 3 years	No plan to export
5～ 9	11,915	1.3	0.8	97.9
15～ 19	6,851	6.5	4.1	89.4
20～ 49	6,482	17.8	13.3	68.9
50～ 99	2,895	33.4	18.0	48.6
100～199	1,825	54.2	12.2	33.6
200～299	720	67.8	9.3	22.9

Source: Survey of Small Business, Ministry of Commerce and Industry, Republic of Korea, 1980.

The above analysis provides an interesting observation that smaller firms with less than 50 employees indicates one of their problems as insufficient sales, but have to limit their scope of sales activities to domestic market. This limitation may be stemming from the structural problems of small business. For the small firms, their production has the following structural characteristics; short production runs, unstabilized engineering design, limited production lines, lack of production standards and incentives, many different and age-old machines in the factory, and non-repetitive operations by each worker.(6) Thus, manufacturing activities in small firms are inefficient and insufficient to satisfy their customers. In addition, marketing cost of small firms is usually higher due to the small size of their sales, and their marketing information is limited to the price, demand, and supply of their products rather than to place focus on needs of their customers. Furthermore, a large number of small firms can offer only one of a few product lines and serve a small market. Also, due to the quality uncertainty, products of small firms are not readily accepted by domestic as well as oversea buyers who tend to favor large, well-established companies. These structural problems affect the small business ability to get involved in the foreign market.

Finally, there are numerous other problems with which small business is confronted when they are involved in export. The following Table-5

(6) Kwak, "An Analysis of Production Structure in Small Firms", *Journal of Small and Medium Industry Promotion*, Vol. III, No. 3, Small and Medium Industry Promotion Co., May, 1982, pp. 5-11.

Table 5. Major problem areas for export by small business in Korea (%)

Number of employees	Rise in manufacturing cost	Lack of oversea market information	Excessive competition	Regulation by importing countries	Inferior quality and design	Raw materials and supplies	Skilled workers	Others
below 50	49.2	10.9	14.7	5.8	7.0	7.5	4.9	—
50 ~199	49.0	13.3	12.9	12.8	5.2	5.4	1.4	—
200~299	52.7	10.5	6.7	9.2	9.7	3.5	2.5	5.2

Source: Survey of Small Business, Ministry of Commerce and Industry, Republic of Korea, 1980.

Table 6. Major problem areas for export by small business in the U.S.
(in order of importance)

1. Gov't or legal requirements
2. Inflation
3. Marketing/product distribution
4. Demand
5. Marketing research
6. Competition
7. Capital/finance
8. Advertising/promotion
9. Pricing
10. Labor/personnel
11. Production
12. Raw materials/supplies

Source: V. Kothaii, "Overcoming the problems of small size in world market."(7)

shows major problem areas for export by small firms in Korea. Table-6 shows problem areas for export by small firms in the U.S.

According to Table-5, the first three categories of problem areas in export activities for small companies in Korea are:

- rise in manufacturing cost
- lack of oversea market information
- excessive competition.

The rest of major problem areas for Korean small firms are:

- regulation by importing countries
- inferior quality and design

(7) Vinay Kothaii, "Overcoming the Problem of Small Size in World Market", 'Proceedings: 24th Annual Conference, International Council for Small Business', Federal Business Development Bank, June, 1979.

- raw materials and supplies
- skilled workers

By coincidence, the U.S. small firms seem to have similar major problems in the first three categories. According to Table-6, except government and legal requirements, the first three categories of problem areas in export activities for small firms in the U.S. are:

- inflation (including rise in manufacturing cost)
- lack of oversea market information (including marketing/product distribution, demand, and marketing research)
- competition

Thus, the above analysis and other evidences point out that success of foreign operations by small business can be attributed to several factors; quality products, reasonable prices, quick response, good understanding of the foreign customer and his environment, specialization by markets or products, adequate amount of capital, perseverance, imagination, and personal touch.(8)

IV. Strengthening the International Competitiveness of Small Business

The above analysis shows that the international competitiveness of small business is at the low ebb due to various reasons and factors. Basically small business is surrounded by unfavorable economic conditions together with weak competitive structure. Under the given condition, it is apparent that small business alone cannot carry out the burden of strengthening competitiveness. There must be joint efforts among small businesses, the industries they belong to (represented by organizations such as co-op or federation of small business), and the government to enhance the international competitiveness of small business.

However, depending upon what measures or actions are needed, small business,

(8) *Ibid.*

the industry, and the government should play different roles and functions. In some cases small business is responsible for major actions while the industries and the government play supportive roles. In other cases, the government should play major roles to strengthen the competitiveness of small business while small business firms actively participate in the government program.

What roles and functions the three different level of organization, i.e., small business, the industry and the government, will play, depends upon the strategic variables and measures which should be taken by them. For example, the above analysis attributed the weak competitive structure of small business to inefficient management, poor product and marketing, and others. This means that some measures must be taken to cope with those problems in small business.

Table-7 shows strategic factors which should be implemented to strengthen the competitiveness of small business and organization level where the major or supportive actions should be executed.

The strategic factors are divided into five categories and each category includes several measures that should be taken to strengthen the international competitiveness of small business. As shown in the Tale-7, most of strategic factors must be implemented by small businesses themselves. It is already asserted that the competitiveness of small business ultimately depends on the initiative, drive, and entrepreneurial ability of individual companies. But, in some case such as oversea sales promotion, small business is not in the position to execute it by itself. In this case, it is more advantageous to conduct such activities on the industry wide base by an association or co-op of the industry. In other measure such as standardization of parts which is necessary to reduce the manufacturing cost, the government will play major role and the industry association will function supportive/supplementary role, and each company should participate in the program.

In general, the government should play major roles in specialization, modernization, and standardization of production and marketing activities and also in the area of administrative matters. The organization of industry such

Table-7. Strategic factors for strengthening international competitiveness of small business

Competitive factor	Level	Enterprise	Industry	Government
General management	Improvement in managerial system	* * *	*	*
	Specialization	* * *	*	* * *
	Establishment of closer relationship with large companies	* *	* *	* * *
	Diversification	* * *	* *	*
Production and technology	Determining size of production facilities	* * *	* *	* *
	Modernization of production facilities	* * *	* *	* * *
	Improvement in productivity	* * *	* *	* *
	Improvement in production techniques	* * *	*	*
	Technical innovation	* * *	*	* *
	Improvement in production process	* * *	*	*
	Strengthening quality control activities	* * *	*	* * *
	Standardization of parts	*	* *	* * *
	Raw material and supplies	* *	* * *	* * *
Marketing/ product distribution	Flexibility with changes in demand	* * *	*	*
	Modernization in distribution	* *	* * *	* * *
	Control on excessive competition	* *	* * *	* * *
	Oversea sales promotion	* *	* * *	* *
	Oversea market information	* *	* * *	* * *
	Pricing policy	* * *	* *	*
Capital/labor	Loans and guarantees for small business	*	* *	* * *
	Adjustment in capital structure	* * *	*	* * *
	Education and training	* * *	* * *	* *
	Skilled workers	* *	*	* * *
	Welfare system	* * *	*	* *
	Labor relation	* * *	* *	* * *
	Job security	* * *	*	* *
	Determination of wage level	* * *	* *	*
Others	Intercompany cooperation	* * *	* * *	* *
	Industrial location	* *	* * *	* * *
	Tax	*	* *	* * *
	Administrative red tapes	*	* *	* * *
	Industrial policy	*	* *	* * *

* * *: major role　　* *: supportive/supplementary role　　*: participative role

as an association or federation should play major roles in the area of joint production and marketing, and intercompany matters. For the rest of strategic factors, small business itself is responsible.

In this paper, detail measures or action programs are not illustrated because they are beyond the scope of the paper. However, the three level of organization must devise appropriate action programs for each strategic factor by considering the conditions surrounding small business in the country.

V. Conclusion

As the world economy gets more interrelated among nations, foreign trade becomes a new challenge for a nation as well as firms in the nation for their survival and growth.

However, due to the salient features of small business, small business' activities in foreign trade has been limited to minimum. It is apparent that small business could not play its proper role in foreign trade because certain preconditions were not met. In this paper, it is attempted to illustrate the problems with which the small business is confronted in foreign trade and necessary measure to strengthen the international competitiveness.

Since most of strategic factors and measures to strengthen the international competitiveness are interrelated and must be a long-term nature, it follows that in most instances they can be achieved only through the joint efforts of small business, the industry, and the government. In this case, each small business must assume major roles in improving its international competitiveness. But, it should be emphasized here that the influence of government is of paramount importance to enhance the international competitiveness of small business. With its tremendous power, the government can build up the weak infrastructure small business is based on and the government should provide financial help, technical assistance, and other types of aid wihch small companies need to expand its marketing activities into foreign trade.