

# A Model Suggestion on Competitiveness and Sustainability of SMEs in Developing Countries

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**Abstract**—The factor which developing countries are in need is capital. Such countries make an effort to increase their income in order to meet their expenses for employment, infrastructure, superstructure investments, education, health and defense. The sole income of the countries is taxes collected from businesses. The businesses should drive profit and return in order to be able to toll. In a world where competition exists, different strategies may be followed by business in developing countries and they must specify their target markets. In order to minimize cost and maximize profit, SMEs have to concentrate on target markets and select cost oriented strategy. In this study, a theoretical model is suggested that SME firms have to act as cluster between each other, and also must be optimal provider for large scale firms. SMEs' policy must be supported by public. This relationship can benefit large scale firms to have brand over the world, and this organization increases value added for developing countries.

**Keywords**—Competitiveness, sustainability, SMEs, developing countries.

## I. INTRODUCTION

ONE of the most significant factors which determine the differences in development level of countries is capital stock. There is a linear relationship between development level and capital stock. Therefore, capital is the mostly needed factor for developing countries to get rid of the underdevelopment process and catch up with developed countries. Underdeveloped countries try to increase their GNI per capita day by day. They need to save capital for their expenses and investment. The main income of the countries is the taxes collected from businesses as these countries have a limited source. The businesses should do some activities to maximize their profit and return in order to be able to ready for competitiveness and sustainability.

Because of existing competition, the businesses in developing countries should practice different strategic applications and also select more strategic targets in order to compete with multinational firms especially with the ones which have variety of brands. The differences between SMEs and large-sized enterprises should be considered in determining the strategies at markets.

In this study, firstly the concept of developing countries, and then the word of competitiveness and sustainability are discussed. And then, a model suggestion is given within the framework of the relations of SMEs among each other and their effect on country development with utilization from

public taking into consideration the strategies that SMEs should follow for integration with large business.

## II. DEVELOPING COUNTRIES

There is a variety of criteria for the classification of countries according to their development level. One of these criteria is Gross National Product per capita. World Bank has classified the world economies as low, middle and high income according to the gross national income (GNI) per capita because of operational and analyst reasons. According to the Atlas Method used for classification by World Bank economies in 2008, it is accepted that those with a GNI per capita less than 975 USD are low income; between 976 USD and 3,855 USD are lower-middle-income; between 3,856 USD and 11,905 are upper-middle-income; and 11,906 USD and more are high income or developed economy [1].

Even if the developing countries which comprise the 84% of world population have spread across different geographical regions, they have similar economic, technologic, political, demographic and cultural features [2]. The features of developing countries are as given below [2], [3]:

- Gross national product per capita is low
- Population of the country is high and population growth rate is rapid.
- Unemployment rate is high
- Income distribution is unfair.
- Agricultural sector has a high percentage in gross national product per capita.
- A chronic foreign trade deficit is seen
- Capital market is not developed enough
- Marginal propensity to consume is high while marginal propensity to save low.

Capital markets in developing countries are not developed enough. One of the main reasons of this is low savings seen as a result of low amount of investments, and accordingly low national income. This situation is a vicious of circle which is self-feeding. The second reason of low savings is that savers prefer to keep the income they got at home; they do not make use of the opportunities of banking systems or invest on stock [4].

The most important reason for the underdeveloped industry sector in underdeveloped or developing countries is the lack of savings and investments. High personal consumption expenditures reduce savings rate, low savings rate tendency cause a reduce in investment rate. When it is thought that the source of capital stock is net investments, it can be easily seen why the capital stock in developing countries is inadequate [5].

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Turkey has had serious improvements in some of the aforementioned features but it is still in upper-middle-income level. Our country which is still having problems in current deficit and external payments is in need of a foreign capital in order to improve employment, complete investments, revive capital market and improve foreign trade. Our businesses should be restructured considering conditions of competition today in order to improve business skills. SMEs which constitute 98% of our businesses should be seriously approached.

### III. SMALL AND MEDIUM SIZED ENTERPRISES

In determining the size of businesses, the criteria such as the area covered, annual sales, balance sheet size, number of the staff, technology being used are considered. However, the number of staff is a practical scale when compared to other criteria so this is the mostly used factor. In our country, different institutions define SMEs in different ways. In this study, the definition by KOSGEB will be considered. According to this definition, a business which has less than 250 staff and do not exceed 40 million Turkish Liras in annual net sales revenue or financial balance sheet is accepted as SME [6].

The definition of SME is, on a large scale, closely related to current problem or the aim the analysis conducted. Different qualitative and quantitative characteristics can be drawn up for SMEs. However, it can be put forward that all SMEs have three common characteristics, being independent, having the characteristics of an enterprise and taking the employer-employee relations in [7].

SMEs have a vital role in the economies of developing countries which cannot make capital savings and do not have large firms that can compete in global market. The existence of SMEs is highly important in terms of adapting rapidly changing market conditions in the globalized world, their role for regional development, lowering unemployment, opening new job fields, contribution to exportation and closing the gap in foreign trade and current deficit [8]. Because of all these mentioned reasons, the importance of SMEs for national economy is increasing day by day and their role in production, exports, added value and investment is reaching a significant size. Even if the foundation and operating of SMEs in Turkey started with the Planned Development Period, their contribution to national economy is understood by 1990. In order to understand the contribution of SMEs to national economy, three key indicators; number of workplaces, employed staff and added value shares, can be seen. In the framework of these qualifications, the importance of SMEs in social and economical fields of Turkey can be understood clearly [9]. SMEs play a key role for economy in Turkey in the fields of employment creation, performing consumer choices easily, product improvement and adding dynamism to manufacturing [10].

The most important contribution of SMEs for developing countries such as Turkey is providing employment. It can be said that SMEs in our country are institutional structures that easily provide employment for more people, open to

technological developments, being influenced from cyclical fluctuations less than large scale firms, adapting to customer changes accordingly structural changes in demand, adapting production process to product diversification. One of the most important problem of developing countries is unemployment, for that reason, the contribution of SMEs to employment is extremely important.

Small and medium enterprises adapt themselves to changes rapidly and revitalize economy as they approach consumer choices flexibly, open to innovation and have a close relationship with the employees [11]. SMEs play source role in changing economy and meet the future requirements [10]. SMEs should grow rationally in order to bring dynamism to the economy. Thompson made five suggestions for small enterprises to grow rationally. It is possible to specify these as [12]:

- To prepare a new and detailed business plan
- To examine cash flow closely through financial advisors
- To ensure the sufficient labor in order to meet capacity increase
- To benefit from advisory services to have objective thinking
- Not to grow quickly and act cautious and restrained

The issues such as growth of SMEs, which have an important place in our economy in terms of employment, added values, etc., getting more profit, becoming a large size business, all these, haunt the dreams of entrepreneurs, also these are significant motivation elements that lead them to success. The place of SMEs in our economic structure in Turkey is well known by everyone. These companies not only create added value, also effective in solution of some local problems such as interregional injustice, etc. The performance by SMEs in recent years bring into question whether a new 'Japan Miracle' will be experienced in Turkey. However, when it is examined closely, it will be seen that these businesses have serious structural problems.

Today, the number of SMEs comprises 98% of the total number of enterprises. SMEs constitute a substantial part of our economy in terms of both employment and capital. This situation is not only seen in Turkey, the same situation can be observed in other developing countries, too. In our country, the employment percentage of SMEs is around 77.8%, their export percentage is around 60% and import percentage is around 40% [13].

### IV. COMPETITIVENESS STRATEGIES AT SMEs

Competitive strategy is defined as presenting a general formula for how a company will compete, what kind of targets they should have and the policies (tools) that should be practiced in order to actualize these targets [14].

The competitiveness of businesses can be determined through a general framework of the methods which are used to analyze the structure of a sector and their competitors. It is stated that the competitiveness in the sector depend on five competitive power of competitive situation in sector and also the relation of business with its environment. These five competitive powers are [14]:

- a) **Threat of new firms that will newly enter into the sector:** New firms obligate others to some competitive behaviors such as waiving from income inevitably and usage of additional resources.
- b) **Bargaining power of customers:** If the customers have bargaining power, they will absolutely use this and the situation will lead a decrease in profit margin.
- c) **Replacement product and service threat:** If there are alternatives for the product and service of the business, this will decrease the profit margin.
- d) **Bargaining power of suppliers:** If there is a power upon the business, the suppliers will increase the prices in a way that will affect the profit margin negatively.
- e) **Competition between the current firms:** Competition will require a decrease in profit margin, new investments in R&D and a decrease in price. It is stated that the average income of a firm in return of investments will be determined with the total of these five competitive powers.

However, in the most general level, three general strategies have been determined to create a defensible position in long term and deactivate the competitors in a sector. These are [14]; overall cost leadership, differentiation and focusing.

1. **Overall cost leadership** requires product or service being offered to the market at a lower price. Quality and service are collateral issues.
2. **Differentiation** provides an additional value to customer, so that customer affords to pay more for these features (design/brand, features, technology, dealer network, customer service, etc.). Cost is not ignored in differentiation yet the primary strategy is making a difference.
3. **Focusing** is such an element which is the combination of overall cost leadership and differentiation, also this targets a specific customer group, product variety or geographical region.

Three general strategies, which are different in terms of function and size, require different sources and abilities, also it is emphasized that it is a must to stick on one of these as a primary target in order to succeed. The situation when a firm cannot improve a strategy in one of these three ways is called "being stuck in between" and this put business which guarantees low profit on the spot.

As a result of globalization, the disappearance of borders in trade caused competitiveness which is seen in both domestic and foreign market affect SMEs as well as large scale enterprises. The competitiveness in world markets is increasing a lot. SMES should keep pace with changes in order to survive and be successful. Because, competitiveness is the most important factor that necessitate organizational change. The need for change which comes to light as a result of globalization affects all the enterprises either great or small. In order to provide a competitive advantage, produce quality products and accomplish the objective it is inevitable for SMEs to follow up investments and changes in terms of administration [15].

## V. SUSTAINABILITY IN SMEs

It might be suitable for the businesses to follow up policies which will make them leader in the market with its prices and enabling competitive power benefiting from cost advantage. SMEs should try to attract attention of their customers in terms of their features with different product, public opinion, technology, service, and quality and production system. Focusing on a certain target and shaping strategies in accordance with these targets may ensure businesses to become an expert and outmatch. Business should be careful while applying this strategy. This is because, if the competitors find another market which is out of firm's target, they can easily exclude the firm. In this scope, presenting product or service in time, increasing quality, being in accordance with standards, creating confidence feeling in customer and increasing staff ability may gain importance. Besides, being aware of the importance of R&D in competition is not enough, businesses should give importance to this in their strategies and practices [16].

SMEs managers mostly give importance to factors about cost. It is expected from the managers who practice cost-oriented strategy to give importance to reducing cost, creating new investment opportunities and maintaining low manufacturing and inventory costs. Especially in developing countries, having a high level risk investment return and resource shortage may cause an inadequate investment of private sector. As well as direct supports of government such as consultation and financing support, indirect supports such as political and economic stability may contribute such businesses. Another problem of SMEs in Turkey is seasonality which is a structural problem. Seasonality causes environmental pressure on local sources at certain time of year and prevents forming a continuous and trained labor force. On the other hand, businesses that fill the entire capacity in certain seasons have a decrease in their profit margin due to inactive capacity. Moreover, they may have problems during market shrinkage due to cyclical economic fluctuations. Another problem caused by seasonality is not being able to create a qualified labor force and having a high staff turnover rate.

## VI. A MODEL SUGGESTION ON COMPETITIVENESS AND SUSTAINABILITY IN SMEs

The SMEs operating especially in industry have financial, skilled labor, marketing, managerial and organizational problems. For the SMEs which are managed by the founders, it is important to benefit from modern management techniques as they are not managed professionally and have low level of capacity usage. Especially KOSGEB can provide free consultancy to SMEs, if possible, they should find a way to benefit from external sources more and national and international networks.

SMEs should assist each other in purchasing materials. If it is possible, they should produce less variety of products with "mass production" so that they can produce goods at cheap, and also they should cluster among themselves to complete product range. By this way, they have the chance to compete

as a result of producing at cheap and going on their existence. Such firms should not attempt to do all the activities all alone and should not get out of its depth. Such firms should both apply cost oriented strategies and become a supplier. On the contrary of SMEs, the large enterprises may apply “differentiation oriented strategy”. In this way, SMEs will become expert in a field, produce goods at cheap and avoid risks, however, larger enterprises will use external sources so that they will not invest unnecessarily, they will use financing effectively and focus on more serious projects.

The SMEs which attempt to do everything on its own, under normal conditions, cause waste of country resources and

affect the market in a negative way. However, it is not easy to change the habits of such business managers. Incentive policies of government may channel SMEs into this way as in South Korea.

The incorporated companies which are accessible to the public should start producing brands in order to increase export and improve the capital market, also large enterprises should be supported with a selective policy to contribute the development of country. Our model about this subject is given in Fig. 1.

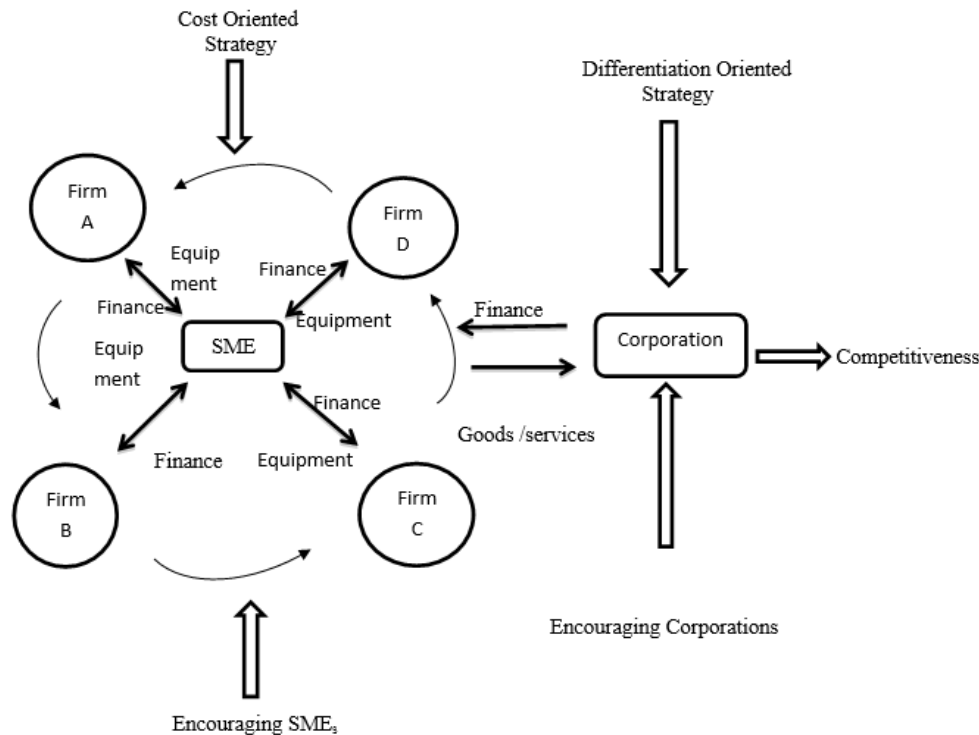


Fig. 1 Integration of SMEs and Large Enterprises

## VII. RESULT AND EVALUATION

The developing countries which comprise the 84% of world population are spread across different geographical regions. Despite being in different regions, developing countries have similar economic, technologic, political, demographic and cultural features. Such countries need a capital intensely in order to solve their problems. It is tried to think of ways to the correct business structures and effective work.

Turkey, our developing country, supports R&D works intensely to produce international brands and innovative products. An effort is made to integrate our law system into international law, also increase the quality of human resources.

The size of the businesses gains importance for public support. KOSGEB can provide free consultancy to SMEs, if possible, external sources can be utilized more and more

efforts can be made to benefit from national and international networks.

SMEs should assist each other in purchasing materials. If it is possible, they should produce less variety of products with “mass production” so that they can produce goods at cheap, and also they should cluster among themselves to complete product range. By this way, they have the chance to compete as a result of producing at cheap and going on their existence. Such firms should not attempt to do all the activities all alone and should not get out of its depth. Such firms should both apply cost oriented strategies and become a supplier. On the contrary of SMEs, the large enterprises may apply “differentiation oriented strategy”. In this way, SMEs will become expert in a field, produce goods at cheap and avoid risks, however, larger enterprises will use external sources so that they will not invest unnecessarily, they will use financing effectively and focus on more serious projects.

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