

**Promoting Coherence in Philippine Policies,
Laws, Rules, and Regulations That Encourage
the Growth and Development of Small and Medium Enterprises
into Active Participants in the Global and Regional Economy¹**

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Abstract

As the Philippines continues to integrate into the global and regional economy, opportunities for growth and development are opened up for small and medium enterprises. However, structural, institutional, legal, and regulatory constraints prevent Philippine SMEs from fully taking advantage of these opportunities, upgrade, and engage in higher value activities. The paper draws attention to gaps in SME characterization that constrains more targeted strategies for growth, coordination problems among implementing institutions, a lack of strategy for SME internationalization, legal and regulatory incoherence, and challenges to SMEs in upgrading and engaging in higher value activities. These gaps should be addressed in a coherent and targeted manner, from the determination of a general policy direction to institutional implementation and legal and regulatory adjustments that should effectively address the identified constraints.

¹ With research and analytical support from Ms. Joan P. Serrano, LLB, and Ms. Jessica Hermosa, MA.

Introduction

With the opening of borders to trade and investment among the Asia-Pacific Economic Cooperation (APEC) economies, the market for micro, small, and medium enterprises (MSMEs) is no longer limited to their individual domestic economies. Global and regional production networks provide opportunities for SMEs to gain access to global markets, in general, and to Asia-Pacific regional markets, in particular.

But APEC economies, especially developing countries like the Philippines, suffer from market failures such as noncompetitive markets, information asymmetries, negative externalities, and limited access to resources and technology, which prevent these SMEs from taking advantage of the potential benefits of liberalized markets and a globalized world.

Government SME policy and implementation should thus be designed to ensure that the advantages and opportunities brought in by trade and investment liberalization and the growing global and regional production networks are maximized for these SMEs. This means that such policy should be mindful of these opportunities, existing market constraints, and have clear targets and directed strategies to maximize these potential benefits and address existing limitations.

The Philippines' hosting of the 2015 APEC Economic Leaders' Meeting is a good opportunity for Philippine policymakers and other stakeholders to take stock of the Philippine SME development policy. With ongoing initiatives at the APEC level, it would be useful to assess whether Philippine efforts and policy directions are compatible with APEC initiatives. As a member of APEC, the Philippines has an opportunity to take advantage and tap into this regional network for support and collaborative activities for SME growth.

However, for the Philippines to be able to maximize partnerships and cooperative activities within APEC, it needs to have a clear understanding of the level of development of its SMEs (and their potential for growth), the impact of existing policy interventions, and gaps that should be addressed by such partnerships and cooperative activities.

One of the main problems cited by numerous studies, particularly in the Philippines, is the weak regulatory environment for business and incoherent laws and regulations that stunt enterprise development. Various surveys have examined the impact of this weak regulatory regime to business. Philippine initiatives to address this are in different stages of development and implementation.

While generally reviewing the results of these studies and ongoing initiatives, this paper does not intend to revisit the matters covered by studies and surveys conducted in the area of regulatory coherence. It will, instead, take a broader view of underlying issues by examining the quality of the processes involved in developing SME policies, the implementation of these policies, and the state of the institutions implementing SME policies.

This paper takes the view that an understanding of the quality of policymaking and implementing institutions and linking these with the quality of business regulations will enrich an understanding of the roots of the problem plaguing SMEs. It could also provide better guidance on how to address the incoherence and arbitrariness of existing regulations.

First, the paper will provide a picture of the general characteristics of Philippine SMEs to provide the reader with a general idea of the capacity of Philippine SMEs to compete in the global environment.

Second, it will review the various aspects of SME development from policymaking, implementation, and institutional development. It will also review the actual constraints faced by SMEs in dealing with business regulations and highlight the need to connect these regulations to a clear policy framework and institutional structure as a means of providing coherence in direction and implementation.

Third, this paper will discuss SME issues in upgrading and engaging in higher value activities in a separate portion given its importance to SME internationalization.

Fourth, the paper will then provide some general recommendations on how to address gaps identified and how to respond to existing challenges.

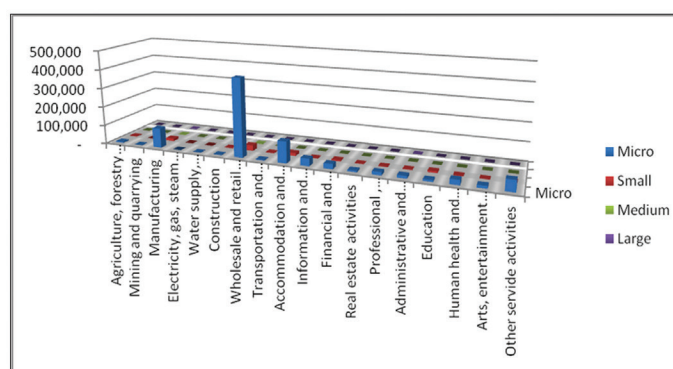
However, given the breadth and scope of the challenges to Philippine SME development and internationalization, this paper will address these areas in general and broad terms, citing illustrative examples where necessary. Further study is necessary in the areas covered for more meaningful insights and guidance in promoting SME growth and engagement in the global economy.

Part I. Philippine SMEs and the Global Economy

A. Characteristics of Philippine Small and Medium Enterprises

As of 2012 (from data released by the National Statistics Office on 18 December 2013), the total number of Philippine establishments is about 945,000. 89.4 percent, or 844,760, of these establishments are microenterprises; 9.7 percent, or 92,025, are small enterprises; 0.4 percent, or 4,136, are medium enterprises; and 0.4 percent, or 4,083, are large enterprises.² A large bulk of microenterprises is engaged in wholesale and retail trade (48 percent), and a significant portion in manufacturing (12 percent), and accommodation and food services activities (13 percent) (see Fig. 1 below). These figures remain substantially similar to 2011 data.

Fig. 1. Distribution of Enterprises Among Philippine Industries (2012)



Source: 2012 MSME Statistics. NSO Website.

In general, however, microenterprises comprise a significant portion of the various industries, particularly in the sectors described above (see Fig. 2), i.e., between 48 percent (water supply, sewerage waste management, and remediation activities) and 95 percent (other service activities) of the total enterprises per industry. Large enterprises make up only between 0.1 percent (wholesale and retail trade) and 9 percent (electricity, gas, steam, and air conditioning supply) of the particular industries.³

The MSME Development Plan 2011-2016, looking back to past years' data, notes that these figures remain unchanged over the past two decades. There is very little evidence of expansion or upgrading of microenterprises to small or medium enterprises. Furthermore, large enterprises continue to compose a minuscule portion of all Philippine enterprises.⁴

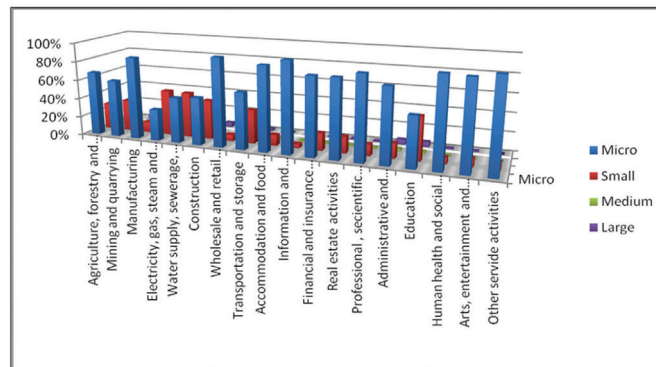
On the other hand, 2011 data show that Philippine enterprises' contribution to

² 2012 Updating of the List of Establishments (ULE): Final Result, NSO Website [<http://www.census.gov.ph/content/2012-updating-list-establishments-ule-final-result>], Accessed 26 December 2013.

³ Calculated from 2012 MSME Statistics.

⁴ Micro, Small, and Medium Enterprise Development Plan, 2011-2016: i.

Fig. 2. Percentage Share of Enterprises to Total Philippine Enterprises (2012)

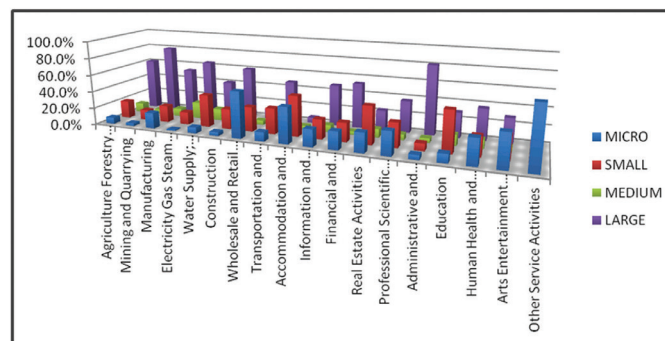


Source: 2012 MSME Statistics. NSO Website.

employment is more mixed (see Fig. 3), although total contribution of SMEs still constitute a significant portion, i.e., about 61.2 percent of the total employment of Philippine enterprises.⁵

While SMEs comprise the majority of all Philippine industries, Table 1, showing 2011 data, indicates that large enterprises contribute more to employment in a significant number of industries than SMEs. For example, while SMEs consist 94 percent of the mining and quarrying industry in 2011, their contribution to employment is only 20.5 percent. Compare this to large enterprises, which consist of only 6 percent of total enterprises, but contribute about 80 percent of total employment. In administrative and support services, SMEs compose 96.6 percent of total enterprises but contribute only around 19 percent of total employment in the industry. In contrast, large enterprises with 3.4 percent of total enterprises contribute 81 percent of total employment.

Fig. 3. Philippine Enterprises' Contribution to Employment (2011)



Source: 2011 MSME Statistics. DTI Website.

⁵ Calculated from 2011 MSME Statistics.

In addition, SMEs contribute only around 35.7 percent of value added,⁶ even while they comprise 99 percent of total Philippine SMEs. This means that the capacity of SMEs to maximize its employment generation potential and to generate more value added has not yet been fully utilized.

The almost stationary trend of SME growth seems to indicate that either SMEs remain micro-, small-, or medium-sized or existing ones close shop to be replaced by similarly sized enterprises that do not upgrade or expand and may also face the same fate of the earlier enterprises. In addition, SMEs, particularly, microenterprises, dominate in wholesale and retail trade, and accommodation and food services. This indicates that current SME capacity, generally, is in trading industries.

The country's SMEs also appear to be moving at a very slow pace compared to its ASEAN neighbors. According to the Philippine Institute for Development Studies (PIDS), a large number of barriers have been the main reasons for this.⁷ In a study conducted by Dr. Rafaelita Aldaba, she observed that the weak performance of Philippines SMEs is attributed to poor access to finance, technology, skills, and information gaps and difficulties in product quality and marketing. Consistent with the data presented above, the study added that while the SME dominated the economy

Table 1. Comparative Schedule of Share in Total Enterprises and Employment Contribution of Enterprises in Various Industries

Industries	SMEs		Large Enterprises	
	Share in Total Enterprises	Employment	Share in Total Enterprises	Employment
Agriculture Forestry and Fishing	97.1%	38.9%	2.9%	61.1%
Mining and Quarrying	94%	20.5%	6%	79.5%
Manufacturing	99.1%	47.2%	0.9%	52.8%
Electricity Gas Steam and Air Conditioning Supply	87.3%	35.3%	12.7%	64.7%
Water Supply; Sewerage Waste Management and Remediation Activities	97.6%	59%	2.4%	41%
Construction	95.6%	39.7%	4.4%	60.3%
Wholesale and Retail Trade; Repair of Motor Vehicles and Motorcycles	99.9%	88.3%	0.1%	11.7%
Transportation and Storage	98.1	52%	1.9%	48%
Accommodation and Food Service Activities	99.9%	93.6%	0.1%	6.4%
Information and Communication	99.5%	51.5%	0.5%	48.5%
Financial and Insurance Activities	99.4%	47%	0.6%	53%
Real Estate Activities	99.4%	76.5%	0.6%	23.5%
Professional Scientific and Technical Activities	99.6%	62.7%	0.4%	37.3%
Administrative and Support Service Activities	96.6%	19%	3.4%	81%
Education	98.5%	70.5%	1.5%	29.5%
Human Health and Social Work Activities	99.6%	63.4%	0.4%	36.6%
Arts Entertainment and Recreation	99.8%	71.2%	0.2%	28.8%
Other Service Activities	99.98%	96.9%	0.02%	3.1%

Source: Calculated from 2011 MSME Statistics. DTI Website.

⁶ Micro, Small, and Medium Enterprise Development (MSMED) Plan, 2011–2016: i.

⁷ The Manila Times, “Barriers hinder growth of SMEs – PIDS,” April 24, 2013 <http://manilatimes.net/barriers-hinder-growth-of-smes-pids/420>.

and had the most number of establishments at 99.6 percent total (microenterprises with 91.6 percent, small enterprises at 0.4 percent, and medium enterprises at 0.4 percent), they all lagged in the share in employment at 61.2 percent and only 35.7 percent of total value added, compared to large enterprises. Firm size also remained unchanged.

The Micro, Small, and Medium Enterprise Development Plan 2011–2016 also notes that SMEs are unable to reach their full potential due to certain constraints such as:

- high cost of doing business,
- lack of access to finance,
- lack of access to market information,
- low productivity, which is largely attributed to a lack of access to technology, weak technological capabilities, and failure to innovate and engage in research and development activities,
- low competitiveness, and
- limited management and financial capabilities.⁸

B. Philippine SMEs and Globalization

The importance of SMEs cannot be overemphasized. In developed and developing countries alike, they are considered as “one of the most important agents of development,”⁹ “the critical success factor” in industrial development,¹⁰ and “a non-negligible force in the national economic development.”¹¹ Much interest therefore surrounds SMEs, and recent studies abound on how they can further contribute to economic development.

Such interest has been generated on the growth trajectories of SMEs. More particularly, many have noted that they fail to “upgrade” or develop. SME studies by Bernet, Gomez, et al. (2008) and Mead (1994) reveal that “a large majority of small enterprises seem to never develop their businesses beyond a certain scale and only a small minority will manage to upgrade their businesses to the next level of productivity, income and employment” and “that across developed and developing economies most micro and small enterprises are in fact stagnating.”¹²

8 MSMED Plan, 2011–2016: i–ii.

9 Altenburg, Tilman, and Eckhardt (2006). Productivity enhancement and equitable development: Challenges for SME development. Combating Marginalization and Poverty Through Industrial Development (COMPID).

10 Choonhaya, Chatichai (1987). “Small Enterprise and Entrepreneurship Development: A Critical Success Factor,” Making Small Enterprises More Competitive Through More Innovative Entrepreneurship Development Programs: Proceedings of the 1st Asia-Pacific Symposium on Small Enterprise and Entrepreneurship Development (SEED Symposium) held in Bangkok and Manila. Singapore: Technonet Asia.

11 Bo, Zhang. Research on SMEs’ Transformation and Upgrading Strategies. Zhang Bo (2010). “Research on SMEs’ transformation and upgrading strategies,” 2010 International Conference on Logistics Systems and Intelligent Management, vol.1, no., pp.404,407, 9–10 Jan. 2010 doi: 10.1109/ICLSIM.2010.5461395.

12 Hampel-Milagrosa, Aimee (2013). Micro and Small Enterprise Upgrading in the Philippines: The

This interest on the failure of SMEs to upgrade is inevitably interlinked with the globalization phenomenon. The Asian Development Bank (2000) describes globalization as the “increased integration of economies around the world through trade and financial flows and movement of labor and technology across international boundaries.”¹³ The International Monetary Fund (2000) calls it the “key to future world economic development and modernization.”¹⁴

Other definitions allude to the interconnectedness of the global and local communities including Roland Robertson’s “compression of the world and the intensification of consciousness of the world as a whole;” Anthony Giddens’s “intensification of world-wide relations which link distinct localities in such a way that local happenings are shaped by events occurring many miles away” and “influence at a distance;” and David Harvey’s “overwhelming sense of compression of our spatial and temporal worlds.”¹⁵ These definitions both emphasize the opportunities provided by this interconnectedness and recognize the challenges and vulnerability of small communities, which includes SMEs, to global developments.

In fact, the SME Development Plan 2004-2010 of the SMED Council cites globalization as a reason why SMEs must be developed. It recognizes the “fierce competition in export markets that globalization has spawned” and acknowledges that its adverse effects on Philippine SMEs is “aggravated by the inability of Philippine SMEs to update themselves with the fast changes on products and manufacturing methods” and “lack the most basic awareness of what globalization is all about”¹⁶ by some mostly “isolated” or informal firms. It admits as well that this situation is made more challenging by “a domestic operating environment that is not sufficiently supportive or conducive to SMEs.”¹⁷

The sentiment prevailing among Philippine SMEs is that globalization puts them at a very disadvantageous position. They believe that they “are vulnerable to various difficulties in a free and open-trading environment. The withdrawal of protectionist measures and other [trade] concessions level[s] the playing field and pits them alongside bigger firms and competitors from other countries.”¹⁸ This reflects a certain risk-averse

Role of Entrepreneur, Enterprise, Networks and the Business Environment. Paper presented at the 2013 Enterprise Performance in Asia Conference by Asian Institute of Management held at the Radisson Blu Hotel, Cebu City, Philippines, on 7-8 November 2013.

13 Asian Development Bank (2000). “Briefing Materials on the 13th Workshop on the Asian Economic Outlook,” Manila, Philippines.

14 International Monetary Fund (2000). “Globalization: Threat or Opportunity,” Washington D.C. USA.

15 Peet, Richard (2004). *Unholy Trinity: The IMF, World Bank and WTO*. Manila: IBON Books.

16 Rodriguez-Co, Myrna (2001). “Getting a Handle on SMEs cum Globalization,” *Bridging the Gap: Philippine SMEs and Globalization*, Oscar M. Alfonso, ed., Quezon City, Philippines: SERDEF and UP ISSI.

17 SME Development (SMED) Plan 2004-2010.

18 dela Peña, Fortunato T. (2001). “Girding their Loins: SMEs Facing Up to the Challenges of Globalization.” *Bridging the Gap: Philippine SMEs and Globalization*, Oscar M. Alfonso, ed., Quezon City, Philippines: SERDEF and UP ISSI.

attitude that arises from a limited understanding of competition in an open market, and a present lack of confidence in their ability and resources to compete.

C. Global Market Developments and SME Internationalization

Globalization has been going on for centuries through trade, foreign investments, and the expansion of operations of multinational corporations. However, from the latter part of the 20th century up to the present, the dynamics of global markets has been quickly evolving. Economies that have been highly protected opened their markets through the lowering of tariffs, deregulation of heavily regulated industries, liberalization and privatization of state corporations. At the same time, information and communications technology has also been rapidly developing.¹⁹

These developments gave rise to at least two changes in the global market: one, the establishment of global production networks as multinational corporations strengthen their competitiveness through maximizing market access opportunities and lower production costs and improved operational flexibility, among others, and two, knowledge transfer to lower-cost markets that have the potential of promoting local capability formation.²⁰

In addition, as the Doha Development Round of negotiations in the World Trade Organization (WTO) reached an impasse, bilateral and regional agreements for the establishment of free trade areas and customs union are becoming the BATNAs, or best alternatives to a negotiated agreement, for most WTO member-countries. Further, certain political and economic issues, such as the dispute over the Spratlys in the Asia-Pacific, the economic crisis plaguing the European Union and the United States, and the rise of China and India, have spurred smaller countries to integrate with its neighbors.

In the Asia-Pacific, regional integration and cooperation are happening in various regional groupings, such as the Association of Southeast Asian Nations (ASEAN)²¹ and the Asia-Pacific Economic Cooperation (APEC).

These developments provide opportunities for growth for SMEs. SMEs are more adaptable and thus more able to meet the changing requirements of global production networks. The competition for market access and low-cost jurisdictions among multinationals also opens markets for SMEs particularly in developing countries like the Philippines.

19 Ernst, Dieter, and Linsu Kim, "Global Production Networks, Knowledge Diffusion, and Local Capability Formation: A Conceptual Framework, Paper presented at the Nelson & Winter Conference in Aalborg, Denmark, June 12-15, 2001, organized by DRUID: 2.

20 Ernst et al., 2-3.

21 ASEAN is going through a process of economic integration through the ASEAN Economic Community (AEC).

D. Analysis and Implications to Philippine SME Internationalization

Based on the discussion above, we have, on the one hand, Philippine SMEs that are characterized by:

- a substantial portion composed of microenterprises (about 89 percent);
- a significant number of wholesale and retail traders (nearly 50 percent of microenterprises);
- stagnation (the composition of SMEs (89 percent, micro; 10 percent, small; 0.4 percent, medium; and 0.4 percent, large) remains unchanged over the past 20 years);
- unresolved constraints that hamper SME growth, such as high cost of doing business, lack of or limited access to finance, information, technology, low productivity and competitiveness, and limited management capabilities; and
- lack of confidence to compete in the global economy.

On the other hand, we have a rapidly evolving global market that provides opportunities to SMEs through global production networks, greater market access through free trade agreements, and the potential for deeper regional cooperation through such regional groupings as the APEC, among others.

Between the current state of Philippine SMEs and the potential for growth offered by current global market trends noted above, there exists a huge gap. In such current state, Philippine SMEs cannot hope to maximize the benefits provided by global markets or to rise up to their challenge.

To bridge this gap, the Philippine government, either through internal initiatives or cooperation with regional groupings such as the APEC, will need to step in. It should act as a catalyst for SME growth through the formulation and implementation of targeted policies, creation of enabling institutions, ensuring coherence in applicable laws, rules and regulations, and strategic cooperation with other economies.

Part II. Aspects of SME Development

In promoting SME growth and development, government intervention must be informed by a thorough consideration of underlying realities, a clear policy direction, a concerted strengthening of enabling institutions, and continuous harmonization of laws and regulations with the basic policy framework.

While this paper is not sufficient to examine these various aspects of SME development in detail, it will provide a general overview of these aspects. The intent is to provide a starting point for deeper analysis and review in subsequent studies for a greater understanding of Philippine SME issues.

We divide these aspects into three:

- A. Policy Development and Implementation
- B. Institutional Development, and
- C. Regulatory Environment.

A. Policy Development and Implementation

From the discussion in Part I above, it is readily apparent that the problem presented involves more than just one perspective. Various disciplines and perspectives are necessarily included in the formulation of policies. An examination of these different perspectives will provide invaluable insights from different viewpoints that would lay the foundation for integrating inevitable conflicts to formulate more targeted policies. For purposes of this study, we will focus on two areas we identified that significantly affect the formulation of a core SME development policy for internationalization in the Philippines. These are:

- 1. defining Philippine SMEs and
- 2. identifying a Core Policy Framework for SME Internationalization.

1. Defining Philippine SMEs

The UNESCAP Policy Guidebook for SME Development in the Asia-Pacific (SME Policy Guidebook)²² notes that SME definitions vary from country to country. Citing a World Bank study, it indicates that about 75 countries use more than 60 definitions of SMEs. Among the most common indicators in defining SMEs are number of employees, annual sales, registered capital, total assets, total credit facilities, and other qualitative indicators.²³

The SME Policy Guidebook observes that SME “definition in each national context facilitates policy interventions, such as the provision of technical assistance, fiscal and financial concessions, and other incentives, which target a specific group of enterprises. It also makes the physical identification of SMEs on the micro level possible, encouraging better articulation of the problems and prospects of the sector.”²⁴ Thus, establishing a clear definition of what constitutes SMEs is the first step in the process of formulating policies, laws, rules, and regulations aimed at promoting their growth and development.

In the Philippines, the definitions of establishments and SMEs under Philippine laws and for statistical purposes vary. Under the Magna Carta for MSMEs (Republic Act

22 Abe, Masato, Troilo, Michael, Juneja, J. S., and Narain, Sailendra, Policy Guidebook for SME Development in Asia and the Pacific, United Nations Economic and Social Commission for Asia and the Pacific (UNESCAP). 2012. Bangkok, Thailand.

23 Abe et al.: 14. See Table II.1.

24 Abe et al.: 14.

6977, as amended by Republic Act 9501), SMEs (also MSMEs) are defined as “any business activity or enterprise engaged in industry, agribusiness, and/or services, whether single proprietorship, cooperative, partnership, or corporation whose total assets, inclusive of those arising from loans but exclusive of the land on which the particular business entity’s office, plant, and equipment are situated,” have the values and the number of employees indicated in Table 2,²⁵ as determined by the MSMED Council.²⁶

But for purposes of updating the List of Establishments in the Philippines, the National Statistics Office (NSO) classifies them according to employment grouping²⁷ as determined by the MSMED Council. However, the NSO includes only enterprises with fixed locations, among others, and specifically excludes other enterprises from the coverage of the survey. These enterprises are referred to as “establishments.”

In conducting its surveys to update the list of Philippine establishments, the NSO defines an establishment as “an economic unit, which engages, under a single ownership or control, i.e., under a single entity; in one or predominantly one kind of economic activity at a single fixed location. Thus, stores, shops, factories, mining companies, electric plants, transport companies, radio stations, hotels, restaurants, banks, insurance companies, real estate development companies and the like are considered establishments Ambulant peddlers and hawkers and movable stalls either along a public road or in a market place, as they do not have a fixed business location, are not considered establishments Similarly, open stalls in shopping centers, malls and markets are not to be listed as they do not have permanency of business location. . . . Individual professionals and technical workers or craftsmen who do not maintain fixed offices or shops are also excluded.”²⁸

The Magna Carta for MSMEs’ definition is quite broad, covering all enterprises engaged in any business activity, which would include establishments expressly excluded by the NSO in its survey of establishments. The NSO definition, on the other hand, is fairly limited and fails to capture microenterprises and most likely some small enterprises that have no registered business addresses.

This means that under the Magna Carta for MSMEs all enterprises engaged in some form of business activity are entitled to its benefits, whether fiscal, nonfiscal, or other advantages provided by underlying policies. However, as can be seen from the Department of Trade and Industry (DTI) website and related studies, the DTI and Bureau of Micro, Small, and Medium Enterprise Development (BMSMED) Council rely on data provided by the NSO, which has limited scope, for policymaking. There is thus an apparent disconnect between the intended beneficiaries of the Magna Carta for MSMEs and the identified potential beneficiaries by the primary data-gathering agency of the government.

25 Republic Act 9501, Sec. 3.

26 SMED Council Resolution No. 1, Series of 2003, dated 16 January 2003.

27 2012 Updating of the List of Establishments (ULE): Final Results, 18 December 2013, NSO Website [<http://www.census.gov.ph/content/2012-updating-list-establishments-ule-final-result>].

28 2012 Updating of the List of Establishments (ULE).

That is not to say that the NSO data have no beneficial use to SME development planning. The data gathered by NSO are a good start off point in generally classifying these SMEs. However, within these classifications would be distinctions brought about by gender, geographical location, levels of education of entrepreneurs, access to resources, and government support, among others. For policy interventions to be effective, these distinctions must be drawn out and the definition/characterization of SME beneficiaries further modified to account for these distinctions.

Note though that from SME reports made by the DTI and MSMED Council, such as the MSMED Plans, there are indications showing that these agencies collect their own data for specific purposes, in addition to the NSO data. However, an examination of the MSMED Plan of 2011-2016, for example, shows that data gathering may be over a limited number of enterprises, such as through stakeholder focus group discussions and/or workshops.²⁹

As indicated in the SME Policy Guidebook quoted above, the definition of SMEs is very important as such definition identifies the intended beneficiaries of SME incentives, and makes possible the physical identification of such beneficiaries. This will, in turn, facilitate policy targeting and interventions.

There is thus a need to review the Philippines' data-gathering capabilities, assess the usefulness of existing data for effective policymaking, monitoring, and evaluation, and identify specific actions moving forward to address existing data-gathering constraints. Ensuring the reliability and sufficiency of data used for policymaking is the first step toward identifying targeted strategies and interventions to support SME growth and development.

The fact that, despite efforts promote SME growth, Philippine SMEs continue to stagnate should inform Philippine policymakers that present efforts are insufficient and that there may be a need to examine the problem beyond operational constraints.

2. Identifying a Core Policy Framework for Philippine SME Internationalization

SME development in the Philippines is primarily pursued through domestic legislation under Republic Act 9501 (2008), otherwise known as the Magna Carta for Micro, Small, and Medium Enterprises (hereinafter "Magna Carta for MSMEs"), which amended an earlier law, Republic Act 6977 (1991). The Magna Carta for MSMEs adopted a policy of promoting, supporting, strengthening and encouraging "the growth and development of MSMEs in all productive sectors of the economy." To achieve this end, it undertakes to:

- intensify and expand programs for training in entrepreneurship and for skills development for labor;
- facilitate their access to sources of funds;

²⁹ MSMED Plan 2011-2016: 21.

Table 2. Classification of SMEs

No.	Enterprise Type	Total Assets	No. of Employees
1	Micro	Not more than PHP 3,000,000.00	1-9
2	Small	PHP 3,000,001.00 to PHP 15,000,000.00	10-99
3	Medium	PHP 15,000,001.00 to PHP 100,000,000.00	100-199

Source: Authors' compilation.

- assure to them access to a fair share of government contracts and related incentives and preferences;
- complement and supplement financing programs for SMEs [MSMEs] and doing away with stringent and burdensome collateral requirements;
- institute safeguards for the protection and stability of the credit delivery system;
- raise government efficiency and effectiveness in providing SME [MSME] assistance, at the least cost;
- promote linkages between large and small enterprises and encourage the establishment of common service facilities;
- make the private sector a partner in SME [MSME] development; and
- assure a balanced and sustainable development through the establishment of a feedback and evaluation mechanism that will monitor the economic contributions as well as bottlenecks and environmental effects of SME [MSME] development.³⁰

The Magna Carta for MSMEs also sets out the principles that will guide government efforts to promote SME growth and development. These guiding principles are as follows:

- a. Minimal set of rules and simplification of procedures and requirements.
- b. Private sector participation.
- c. Coordination of government efforts.
- d. Decentralization. SME development efforts will be dispersed through regional and provincial offices for greater efficiency in implementation and coordination with local government units.³¹

30 Republic Act 6977, Sec. 2, as amended by Republic Act 9501.

31 Republic Act 6977, Sec. 5, as amended by Republic Act 9501.

To achieve this end, the Magna Carta for MSMEs directs the Department of Trade and Industry to prepare periodic six-year MSME Development Plans (the “MSMED Plan”), which shall be approved by the President of the Philippines and shall form part of the periodic Philippine Development Plan.³² The MSMED Plan implements the policy direction and objectives set out in the Magna Carta for MSMEs, which essentially focus on addressing the operational constraints affecting business growth and development in the Philippines.

a. Implementation of SME Development Plans

The Small and Medium Enterprises Development Plan 2004–2010 (SMED Plan 2004–2010)³³ set out to assist SMEs in graduating to “higher levels of business undertakings and upgrading their productivity and value added capabilities”³⁴ for the implementing period 2004–2010. This is an implicit acknowledgment of the challenges and opportunities presented by the changing global market environment referred to in Part I above.

Midway through the implementation of the SMED Plan 2004–2010,³⁵ the DTI implemented a results-based management (RBM) approach. This was intended to mainstream the results-based management at the national and local levels, harmonize the development agenda and monitoring and evaluation at these levels, and encourage participatory planning among various stakeholders.³⁶

The SMED Plan 2004–2010 was implemented through various strategies and activities, which included (i) streamlining business registration requirements at the local government unit level and selected national agencies; (ii) granting loans to various MSMEs; (iii) promoting the One-Town-One-Product Program; (iv) organizing local and international trade fairs; (v) buyer-supplier matching assistance; (vi) product research and development assistance; (vii) technology training and technology transfer and commercialization assistance; and (viii) packaging and labelling assistance. These strategies and activities were streamlined into four outcome portfolios: (a) Business Environment, (b) Access to Markets, (c) Access to Finance, and (d) Productivity and Efficiency.³⁷

32 Republic Act 6977, Sec. 6, as amended by Republic Act 9501.

33 This was crafted under the old law, Republic Act 6977, where these enterprises were referred to as small and medium enterprises, or SMEs. The new law, Republic Act 9501 modified the term to “micro, small, and medium enterprises,” or MSMEs.

34 MSMED 2011–2016: 12.

35 In 2007.

36 This approach was meant to “mainstream results-based management to national and local stakeholders; build the capacity of these stakeholders to manage results; harmonize national and local MSME development frameworks and their concomitant M&E frameworks; and implement a participatory development approach through a combination of the top-down with bottom-up development planning.” MSMED Plan 2011–2015: 15.

37 MSMED Plan 2011–2016: 12–15.

The DTI and Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ, formerly GTZ) conducted a joint evaluation study of the results of the various strategies and activities adopted under the SMED Plan 2004–2010 and made the following relevant findings (see Table 3).

The Micro, Small, and Medium Enterprises Development Plan 2011–2016 (MSMED Plan 2011–2016) crafted under the Republic Act 9501 continues the four outcome portfolios established during the implementation period of SMED Plan 2004–2010. It aims to generate employment of 2 million and raise the economic contribution of MSMEs to 40 percent³⁸ of Gross Value Added (GVA) by 2016 to make it at par with the rest of the countries in the region.³⁹

To achieve these goals, the MSMED Plan 2011–2016 established a results framework drawn from a series of workshops among various stakeholders (see Table 4).

The MSMED Plan 2011–2016 then adopted three approaches to achieve these results framework, as follows:

- following a Local and Regional Economic Development Approach; it aims to harness the competitive advantage of a locality by ensuring (i) that decisions and actions are made, as far as practicable, at the local government level⁴⁰ and (ii) the participation of all relevant stakeholders,⁴¹ particularly the private sector, in decision-making.⁴²
- it promotes the development of relevant value chains, such as manufacturing and service processes, that go beyond a focus on product or industry-based interventions (a Sector Development Approach). This is intended to ensure the sustainability of industries through increased effectiveness of supply and distribution channels.⁴³
- it adopts a Market System Development Approach, where market players are enabled to participate in the market and government intervention is focused on improving the efficiency of the market.⁴⁴

Taking into consideration the current trends in globalization and regional integration, as discussed in Part I above, the MSMED Plan 2011–2016 also encourages the incorporation of four thematic areas in provincial action plans that it identified as relevant to contributing to MSMEs global competitiveness. These areas are:

38 From the current level 35.7 percent.

39 MSMED Plan 2011–2016: 26.

40 The principle of “subsidiarity” where decisions are devolved to the lowest practical level. The Free Dictionary. Available at <http://www.thefreedictionary.com/Principle+of+subsidiarity>. Accessed 5 July 2014.

41 The principle of “participatory development.”

42 MSMED Plan 2011–2016: 32–33.

43 MSMED Plan 2011–2016: 33–34.

44 MSMED Plan 2011–2016: 34.

Table 3. Evaluation of SMED Plan 2004-2010

Subject Matter	Accomplishments	Areas for Improvement	Recommendations
Four outcome portfolios	Building of goodwill, synergies, and better preconditions for effective implementation of a national MSME strategy resulting from improved interaction and dialogue between stakeholders		
	Overall four outcome portfolios are well chosen		Maintain these outcome portfolios moving forward, with a few adjustments in response to the findings below
Access to Finance	Improved access to finance	Smaller MSMEs are benefiting less than the more established ones	Further development of policies for bankability of MSMEs
Productivity and Efficiency		Challenges in investing in skills, technology and quality	Build up more professional knowledge to counsel MSMEs
	Diversified, accessible, and professional productivity-related services		Links between services related to productivity and market access need stronger focus
Access to Markets		Less priority given to finding access to markets	Links between services related to productivity and market access need stronger focus
Harmonization of national and subnational SMED Plans	Improved coordination of support activities that encouraged cooperation, improved interaction and trust between provincial and national levels	<ul style="list-style-type: none"> • Low awareness of SMED Plan • Difficulty of attributing observed improvements to the SMED Plan • Lack of documented success stories • Differences in between MSMEs and enablers on required support services 	

Stakeholder View of the SMED Plan		<ul style="list-style-type: none"> • Understood as an umbrella, but not as a strategy providing new directions • Agencies have their own budgets and plans, which will continue even without the SMED Plan • BMSMED's M&E formats are complicated and taxing 	<ul style="list-style-type: none"> • Need for impact monitoring • More feedback from BMSMED
Growth of MSMEs	<ul style="list-style-type: none"> • Improved turnover (sales) • Growth of smaller and larger MSMEs 	<ul style="list-style-type: none"> • No improvement in employment • Low investment activity • No growth among medium sized enterprises 	
Product improvement	There is improvement in product/service quality and reduced prices in the past	Growing competitive pressure	Diversify, modernize, improve skills and investment in modern technology
Access to credit		Little improvement in access to credit	
Enterprise establishment	<ul style="list-style-type: none"> • More enterprises being set up • Better public private cooperation 		
Sustainable MSME growth		<ul style="list-style-type: none"> • High cost of doing business • Imperfect capital market • Weak competitiveness • Lack of strong coordination among national agencies and local government units weakened implementation 	On poor coordination, evaluate programs to improve decision making at all levels, i.e., management, policy, and budget allocations

Source: MSMED Plan 2011-2016, 18-20.

Table 4. MSMED Plan 2011-2016 Projected Outcomes

Outcome Portfolios	Results Framework
Business Environment (BE) ⁴⁵	<ul style="list-style-type: none"> • The cost of doing business (taxes, fees, etc.) is affordable to MSMEs. • The institutional support structures for the development of startup and existing MSMEs are in place. • The policies necessary to develop the MSME sector are crafted and being fully implemented. • Support for MSME development is results based, coordinated, harmonized, and sustained by capable stakeholders. • An entrepreneurial mindset is pervasive among MSMEs and other MSME stakeholders. • Soft and hard infrastructures for MSME development are established. • The information needs of MSMEs are available and accessible. • MSMEs are gender responsive and environment friendly.
Access to Finance (A2F) ⁴⁶	<ul style="list-style-type: none"> • The financial products, services, and support programs that MSMEs need are sustainably available even to startup MSMEs and MSMEs operating in the countryside. • The cost of obtaining MSME loans is reasonable and affordable. • The requirements that MSMEs need to comply with to obtain loans are reasonable and manageable. • The process that MSMEs need to follow and documents that must be submitted to obtain loans are simplified and streamlined. • MSMEs are trained in financial management and are able to understand and speak the language of financial institutions, while financial institutions are trained to understand and speak the language of MSMEs. • Financial products and services for MSME lending are gender responsive and environment friendly. • The information needed by MSMEs to access financial resources are available and easily accessible. • The assistance extended by stakeholders to MSMEs in accessing funds are coordinated, relevant, and effective.

45 “Business Environment is a dynamic practice and culture of governance that fosters the establishment, development, sustainability, and competitiveness of socially responsible and environment-friendly MSMEs.”

46 “Access to Finance is the sustained availability of reasonably priced, socially responsible, and environment-friendly financial products, services, and support programs that are designed for MSMEs and that MSMEs can conveniently and readily access.”

Access to Markets (A2M) ⁴⁷	<ul style="list-style-type: none"> • MSMEs have maintained their existing markets and penetrated new and emerging markets locally and globally. • MSMEs are competitive locally and globally. • Marketing support systems are established and are operating on a sustainable basis. • MSMEs are implementing the value chain approach and are highly benefited by it. • MSMEs are using information technology and intellectual property system to develop a sustainable market share and gain competitive advantage for their products and services. • Market information needed by MSMEs is available and freely accessible. • MSMEs have considerable market share in the sustainable development market locally and globally. • Government support programs to help MSMEs access local and global markets are coordinated and highly satisfactory.
Productivity and Efficiency (P&E) ⁴⁸	<ul style="list-style-type: none"> • Government programs and policies on productivity enhancement are coordinated, effective, and highly satisfactory. • The MSME workforce is highly motivated and is equipped with the appropriate skills and attitude needed by MSMEs. • The working environment of MSMEs fosters greater productivity and efficiency among the workforce. • MSMEs are using gender-responsive and environment-friendly technologies. • MSMEs are compliant with international quality standards. • MSMEs are using state of the art productivity enhancing technologies. • Information on productivity enhancement is available and freely accessible to MSMEs.

Source: Micro, Small, and Medium Enterprises Development Plan 2011–2016.

47 “Access to Markets is the sustained ability of MSMEs to be competitive in selling their products and services to existing and new markets, both domestic and international, under a climate of fair, free, socially responsible and environment-friendly trade practices.”

48 “Productivity and Efficiency refers to the production and delivery of competitive, standards-compliant, socially responsible, and environment-friendly products and services that generate optimum economic returns.”

- Gender mainstreaming. Consider differences in access to resources and opportunities of women and men that arise from gender roles.
- Migration. Maximize the investment potential of remittances and increased knowhow of Philippine overseas foreign workers (OFWs).
- Climate change / green growth. Take advantage of opportunities from increased demand for “green products.”
- Corporate Social Responsibility (CSR) and linkages with large companies. Improve existing linkages with large domestic and multinational corporations and take advantage capacity building and technology transfer programs of these companies to help MSMEs improve their competitiveness.

b. Analysis and Implications to Philippine SME Internationalization

The most recent SME development plans have been progressively classifying focus areas that are substantially providing clarity in the direction of SME development policy. It is also notable that the SME plans are hewing closely to the guiding principles provided by the Magna Carta on MSMEs:

- a. Minimal set of rules and simplification of procedures and requirements. Reflected in extensive efforts to streamline business registration procedures at the LGU level.
- b. Private sector participation. Involvement of private sector representatives in workshops and focus group discussions to identify existing constraints for MSMEs and in the formulation of development plans.
- c. Coordination of government efforts. Involvement of LGUS and relevant national government agencies in development planning.
- d. Decentralization. The SME development plans, particularly, the MSMED Plan 2011–2016, explicitly leaves the formulation of local SME development plans to responsible local government units. The MSMED Plan 2011–2016, for example, simply provides a general framework for development planning, as illustrated through its results framework, approaches to development, suggested thematic areas.⁴⁹

However, the plans tend to spread resources too thin, and they focus on too many areas at the same time while trying to deal with existing market, systemic, and institutional constraints.

This can be observed from the findings of the joint evaluation study conducted by the DTI and GIZ for the implementation period 2004–2011, some of which we highlight below:

⁴⁹ Republic Act 6977, Sec. 5, as amended by Republic Act 9501; see MSMED Plan 2011–2016.

- Despite efforts to improve MSME access to finance through the grant of loans, smaller MSMEs are benefiting less than more established ones.
- Despite efforts to promote SME growth, medium-sized enterprises show a noticeable lack of growth.

The fact that smaller MSMEs are not benefiting from access to finance initiatives, and medium-sized enterprises show no improvements in growth, indicates that this group of enterprises may require different interventions. This is an example of why there is a need to clearly define the SMEs to which development policies are directed (see discussion in Part II.A.1). It is not enough to conduct a general survey of enterprises defined by total assets and number of employees. These indicators may be a good starting point, but as results of policy interventions become apparent, there is a need to conduct impact assessments and further define these enterprises based on identified differences.

Otherwise, government resources may be unnecessarily wasted in blindly pursuing programs and policy interventions that do not have any or limited impact.

- There are continuing challenges in investing in skills, technology and quality.
- There is less priority given to market access.

The challenges in investing in skills, technology and quality, and market access indicate that these areas are not given as much priority in terms of allocating existing resources. Further study is required to understand the special difficulties in these areas that hold back more significant progress.

- Challenges in monitoring and evaluating the progress of relevant programs and activities that is reflected, for example, in the difficulty in attributing observed improvements to the SME development plans.

These challenges indicate that the monitoring and evaluation (M&E) system of the MSME Council is not as robust as required and is in need of further improvement. It bears emphasizing that M&E, which includes benchmarking, in any project or program of development is one of the most important aspects of program implementation. Without an effective M&E, resources are wasted needlessly, gaps and impacts are not effectively measured, and programs generally suffer from a lack of direction.

- Weak implementation of programs and activities due to lack of strong coordination among national agencies and local government units.

The responsibility for SME development in the Philippines is dispersed among various local and national government agencies and private sector representatives. (See discussion in Part II.B.) This

makes coordination in implementing SME development programs and activities a challenge. Because several parties are responsible for the implementation of SME development plans, the responsible institutions should either make a concerted effort to strengthen coordination or such institutional structure should be reviewed and alternative mechanisms should be considered.

The findings highlighted above indicate that for every gap or limitation identified, in most cases, more work is needed to address these. This could be, either through targeted studies, change in policy direction, institutional reform, or implementation of responsive strategies, programs and activities, among others. However, nowhere in the MSMED Plan 2011-2016 is it indicated that these identified gaps are being addressed and how.

In addition, while following the identified four outcome portfolios in the SMED Plan 2004-2010, the results framework of the MSMED Plan 2011-2016 is too broad and seems geared for longer timelines than the five to six-year year period covered by the plan.

A review of the programs and projects initiated under the SMED Plan 2004-2010 by the DTI together with various public and private stakeholders indicates that most efforts are focused on streamlining business registrations, supporting startups, and clustering initiatives through the One-Town-One-Product program that emphasizes production of food and agricultural products. There is not as much substantial effort put into research and development and diversification into other potentially globally competitive goods and services.⁵⁰

These efforts are inconsistent with the avowed goal of SMED Plan 2004-2010 and continued in MSMED Plan 2011-2016 of assisting SMEs in graduating to “higher levels of business undertakings and upgrading their productivity and value added capabilities.”⁵¹

It seems that the problem again goes back to finding an effective definition of Philippine SMEs. Most efforts are geared toward assisting business start ups and micro or small enterprises. While these are essential to promoting SME growth and development, it is evident that Philippine micro and small enterprises are still a long way from being able to upgrade or compete in the global market.

Philippine policymakers may consider rethinking the basis of analyzing the readiness of SMEs, first, to start and operate a business in the Philippines and, second, to compete in the global market.

50 MSMED Plan 2011-2016, Appendix 2: 49-69.

51 MSMED Plan 2011-2016: 12.

A useful framework for analyzing the readiness of SMEs to participate in the global economy is an APEC commissioned study, titled “Study on SME Internationalisation Best Practices Across Selected APEC Economies” (the APEC SME Study).⁵²

The surveys sought to identify the best practices, demand and supply gaps, and low focus areas in these SMEs and classified these into:

- (a) Readiness – “highlights preinternationalisation issues in terms of the available assistance and policies that provide SMEs with the necessary financial help, market knowledge and human resources to venture overseas;”
- (b) Implementation – evaluates the effectiveness of the “actual implementation” and its necessary procedures in establishing a presence in foreign markets by focusing on both environment and implementation issues that will either expedite or impede on the internationalisation process;” and
- (c) Growth – “entails the mapping and analysis of available programmes necessary to sustain and consolidate SMEs’ operations on both short and long-term basis during the postinternationalisation phase.”⁵³

If we define/classify SMEs according to the above framework, it would appear that SME development initiatives have been primarily focused on the readiness of SMEs to operate as businesses (preinternationalization issues) and not to upgrade or engage in higher value activities to compete or participate in the global market.

In the first place, are Philippine SMEs, as defined by present laws and surveys, ready to compete? Are there other business entities not covered by existing definitions that may be in a better position to compete or participate in the global market or internationalize?

Once these distinctions are identified, it would be much easier to formulate SME development policies and distinguish those that are intended to advance Philippine SME’s readiness, first, to establish and operate in the Philippines and, second, to upgrade or engage in higher value activities to participate in the global market.

Note that a policy to assist SMEs to internationalize should not necessarily be the entire SME development policy. Opportunities in the domestic market abound. But with current global market trends, greater opportunities have opened for Philippine SMEs. These opportunities present their own unique set of problems, and thus special attention should be given to it, distinct from the existing SME development plans.

B. Institutional Development

Among the findings in the joint evaluation study for SMED Plan 2004-2010 is the

52 APEC (2011). Study on SME Internationalisation: Best Practices Across Selected APEC Economies, APEC Publication No. 211-SM-01.2, June 2011. Available at http://publications.apec.org/publication-detail.php?pub_id=1170. Accessed 8 June 2014.

53 APEC (2011): 6.

weak implementation of programs and activities due to lack of strong coordination among national agencies and local government units. This is due primarily to the way implementing institutions for SME development are set up.

Under the Magna Carta for MSMEs, the Micro, Small, and Medium Enterprise Development (MSMED) Council (formerly the “Small and Medium Enterprise Development (SMED) Council” under Republic Act 6977) is primarily responsible for facilitating and coordinating efforts of various government agencies to promote the growth and development SMEs. It is also mandated to review existing SME development policies and initiatives, monitor and evaluate related initiatives, and recommend changes in policies where necessary⁵⁴ to rationalize existing SME Programs and Agencies.⁵⁵

The MSMED Council is attached to the Department of Trade and Industry. The Bureau of Micro, Small, Medium Business Development, another DTI attached agency, is designated as the Council Secretariat to assist the MSMED Council in the execution of its functions.⁵⁶

The implementation of the law, however, is dispersed among various government agencies and instrumentalities. There are as many implementors of SME laws as there are government agencies tasked or mentioned under the law. At the helm of implementation of the MSME laws is the Department of Trade and Industry (DTI), to which the MSMED Council is attached. Within DTI are the following implementing offices:

- DTI Regional Operations and Development Group (RODG)
 - Bureau of Micro, Small, and Medium Enterprises Development (BMSMED) – MSMED Council Secretariat
 - One Town, One Product (OTOP-Philippines)
 - Cottage Industry Technology Center (CITC)
 - 16 DTI regional offices and 81 provincial/city/area DTI offices assist the local government units (LGUs) in developing their respective MSME development plans
- DTI Industry and Investments Group (IIG)
 - Board of Investments (BOI) – assists the LGUs in their investment plans
 - Small Business Corporation – DTI attached agency created under RA 9501

As the coordinating body for MSME initiatives within the DTI, the MSMED Council is composed of the following:

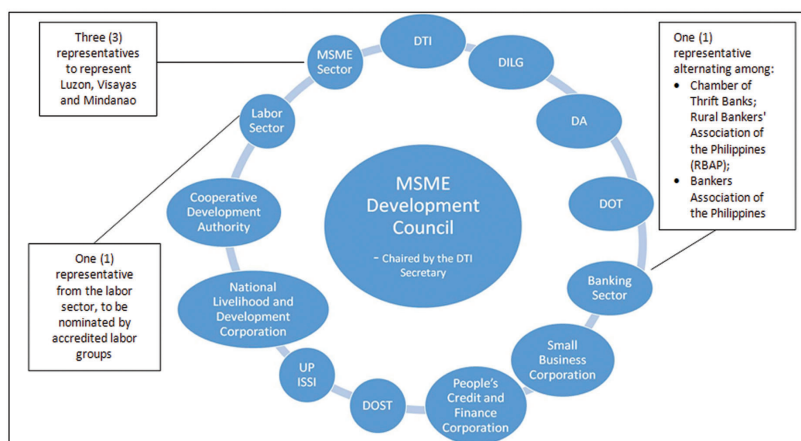
54 Republic Act 6977, Sec. 7-B, as amended by Republic Act 9501.

55 Republic Act 6977, Sec. 7-B, as amended by Republic Act 9501.

56 See Republic Act 6977, Sec. 8, as amended by Republic Act 9501.

- Chairman: Secretary of DTI
- Members:
 - Secretary of Department of Agriculture (DA)
 - Secretary of the Department of Interior and Local Government (DILG)
 - Secretary of Department of Science and Technology (DOST)
 - Secretary of Department of Tourism (DOT)
 - Chairman of Small Business Corporation (SBC)
 - Three representatives from the MSME sector to represent Luzon, Visayas, and Mindanao
 - One representative from the labor sector, to be nominated by accredited labor groups
 - A representative from the private banking sector to serve alternately among the Chamber of Thrift Banks (CTB), the Rural Bankers' Association of the Philippines (RBAP), and the Bankers Association of the Philippines (BAP)
 - Cooperative Development Authority (CDA)
 - National Livelihood and Development Corporation (NLDC)
 - People's Credit and Finance Corporation (PCFC)
 - University of the Philippines Institute for Small Scale Industries (UP ISSI)

Figure 4. Members of the MSMED Council



Source: Unpublished manuscript of Joan P. Serrano

Section 4 (on Guiding Principles) of Republic Act 9501 also mandates the coordination of government efforts to achieve coherence in objectives, and as such, all appropriate offices shall provide the necessary support and assistance to MSMEs, in particular:

- Department of Trade and Industry
- Department of Finance
- Department of Budget and Management
- Department of Agriculture
- Department of Agrarian Reform
- Department of Environment and Natural Resources
- Department of Labor and Employment,
- Department of Transportation and Communications
- Department of Public Works and Highways
- Department of Science and Technology
- Department of Interior and Local Government
- Department of Tourism
- National Economic and Development Authority,
- Philippine Information Agency
- Bangko Sentral ng Pilipinas
- All Local Government Units, which, under the Local Government Code, have:
 - o Sangguniang Bayan, Panlungsod, and Panlalawigan; and
 - o Provincial, City, Municipal, and Barangay Development Council

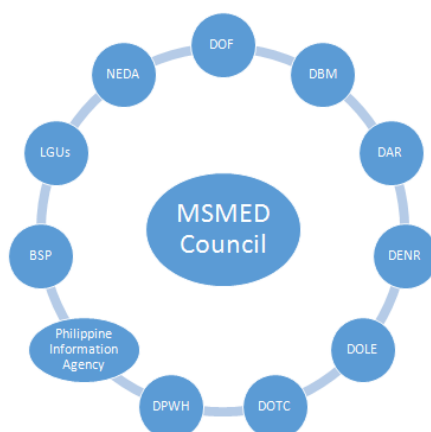
The government agencies and instrumentalities enumerated above are assigned responsibilities among the four focal points outlined in the MSMED Plan 2011–2016, namely, (1) Business Environment, (2) Access to Market, (3) Access to Finance, and (4) Productivity and Efficiency.

To make the business environment more friendly and conducive for MSME growth and development, efforts are made to streamline the business regulatory requirements and processes. There is the ongoing effort spearheaded by the National Competitiveness Council (NCC) in cooperation with the Department of Trade and Industry (DTI) and Department of Interior and Local Government (DILG) to decrease the number of days and steps in the application and renewal of business permits and other business forms.⁵⁷ There is also the effort to establish the Philippine Business Registry Databank, which “will be the repository of information on business enterprises in the Philippines” and “will promote and expand trade and investment through electronic information networking.”⁵⁸

57 National Competitiveness Council website <http://www.competitive.org.ph/doingbusiness>.

58 Senate Bill 169. An Act Authorizing the Establishment of a Philippine Business Registry Databank. Senate of the Philippines. 16th Congress.

Figure 5. Implementors Who Are Nonmembers of the MSMED Council



Source: Unpublished manuscript of Joan P. Serrano.

On the other hand, to enhance support to MSMEs' access to market, the Bureau of Domestic Trade, the Bureau of International Trade Relations, Center for International Trade Expositions, and the Foreign Trade and Service Corps of the DTI provide relevant assistance. The Department of Agriculture (DA) also has the Agribusiness and Marketing Assistance Service, which showcases various agri-fishery products. In terms of design needs and requirements, DTI also has the Product Development and Design Center of the Philippines (PDDCP) along with Department of Science and Technology's Industrial Technology Development Institute with its packaging research and development service.

To improve access to finance, the Philippine government has a motley of microfinancing and SME lending programs.⁵⁹ DTI increases awareness of these programs through the publication of a compilation showing the program objective, features, qualifications, and documents required of potential borrowers as well as the terms and conditions of the programs.

To boost productivity and efficiency, on the other hand, various productivity programs have been initiated by various government agencies. For example, the Department of Labor and Employment initiated the Productivity Olympics. The Olympics is a biennial national competition of best productivity programs of MSMEs launched by DOLE National Wages and Productivity Commission (NWPC) in 2008 to intensify national awareness and commitment to quality and productivity.⁶⁰ MSMEs are categorized by sector (agribusiness, industry, and service) across establishment size

⁵⁹ Department of Trade and Industry (2012). Financing Program for MSMEs.

⁶⁰ Pamphlet published by Information and Publication Division of the National Wages and Productivity Commission.

(micro, small, and medium) and their productivity programs are assessed by regional and national judging panels on the basis of their impact on business performance and resource management.⁶¹

The Integrated Productivity Framework or the ladderized consolidated training program has been effected since 2010 and provided at no cost to the MSME beneficiaries.⁶² This includes the ISTIV module and the ISTIV Plus module, the Service Quality for Hotels and Restaurants Industry Program covering the value chain of the tourism industry, the Green ME (My Enterprise) Program, and the new labor law compliance system.⁶³ A new training program on innovation and enterprise development involving the DTI and the Department of Science and Technology (DOST) is also underway.⁶⁴

To improve access to technology, the Department of Science and Technology has the Advanced Science and Technology Institute (ASTI), the Technology Application and Promotion Institute (TAPI), the Technology Resource Center (TRC), the Science and Technology Information Institute (STII), and the Industrial Technology Development Institute (ITDI) to foster technology transfer and assistance and technology promotion and information dissemination.⁶⁵

Among the programs and services of these institutes include the Small Enterprise Technology Upgrading Program (SET UP) where technological assistance is given to qualified SMEs and the Manufacturing Productivity Extension (MPEX) Program where consultants are fielded to assist MSMEs in improving productivity through technology.

Analysis and Implications to Philippine SME Internationalization

Because of the way the implementing institutions for SME development are set up, the MSMED Plan 2011–2016 adopted the portfolio management approach. This entails the creation of more bodies and committees at the local government level that will work as coequal stakeholders of the bodies and agencies already identified above.⁶⁶

It is notable that the finding of weak coordination among implementing institutions under SMED Plan 2004–2010 was not directly addressed by the MSMED Plan 2011–2016. In fact, another layer of committees was set up that could potentially aggravate the coordination problem.

⁶¹ Ibid.

⁶² Department of Labor and Employment Secretary Rosalinda Dimapilis-Baldoz, Keynote Speech in the 2013 Productivity Olympics Awarding Ceremonies held at the Century Park Hotel, Manila on 24 October 2013.

⁶³ Id.

⁶⁴ Department of Labor and Employment Secretary Rosalinda Dimapilis-Baldoz, Keynote Speech in the 2013 Productivity Olympics Awarding Ceremonies held at the Century Park Hotel, Manila on 24 October 2013. Ibid.

⁶⁵ <http://www.dost.gov.ph>.

⁶⁶ MSMED Plan 2011–2016: 38–39.

Another consequence of having only a coordinating body with numerous implementing agencies is that even the quality of data or information gathered may not be completely accurate, relevant, or necessary to the overall SME development plan. Based on a reading of the MSMED Plan 2011-2016, information (other than data gathered from surveys) is gathered through workshops and focus group discussions.

While this is necessary to promote the participatory process mandated under the Magna Carta for MSMEs, the information gathered does not pass through a verification process by experts or people knowledgeable of Philippine SME concerns. This would mean that information gathered in one or two workshops by one implementing body would most likely be considered true in all cases and become the basis for the formulation of targeted strategies and programs. This is when these strategies and programs become unresponsive to SME needs and result to a needless waste of resources.

Unfortunately, given the state of the law, these are challenges that cannot be effectively addressed at the agency or department level. A review of the law and current institutional structures may be necessary to address identified constraints.

C. Legal and Regulatory Environment

The legal structure of SME development, particularly with respect to policy and institutional frameworks, are discussed in Parts II.A and II.B above. This portion will address how existing laws and regulations encourage or discourage the growth of SMEs.

We divide the discussion into two:

1. Legal incentives to promote SME growth and
2. Challenges to ease of doing business. This paper will focus on ease of doing business as surveys and studies focused on this cover most of the regulatory aspects of doing business in the Philippines.

1. Legal Incentives to Promote SME Growth

To promote the growth and development of SMEs, Philippine laws, primarily the Magna Carta for MSMEs, provided benefits and incentives to SMEs. Among these are the following:

- Creation of the Small Business Guarantee and Finance Corporation or Small Business Corporation (“SB Corporation”) to assist MSMEs in all areas including, but not limited to, finance and information services, training, and marketing.⁶⁷
- Option to establish a Venture Capital (the “Venture Capital Fund”) and Micro Finance Trust Fund (the Micro Finance Fund”) through

⁶⁷ Republic Act 6977, Sec. 11, as amended by Republic Act 9501.

the SB Corporation. The Venture Capital Fund shall be used to primarily finance technology-oriented industries, while the Micro Finance Fund shall be used to provide collateral-free fixed and working capital loans to micro and small enterprises.⁶⁸

- **Mandatory Allocation of Credit Resources to SMEs.** Until 2018, all lending institutions as defined under *Bangko Sentral ng Pilipinas* (BSP) rules, whether public or private, are required to set aside at least 8 percent for micro and small enterprises of their total loan portfolio based on their balance sheet as of the end of the previous quarter and make it available for MSME credit. Compliance may be through any of the following:
 - a. extension of loans to eligible SMEs;
 - b. subscription of preferred shares of shares of stock of the SB Corporation;
 - c. wholesale lending to Participating Financial Institutions (PFIS) for on-lending to SMEs;
 - d. purchase/discount of SMEs receivables; or
 - e. loans granted to SME export, import, and domestic traders;
 - f. subscription or purchase of liability instruments as may be offered by the SB Corporation.⁶⁹

Under Republic Act 6977 (1991), the earlier SME law, lending institutions that do not comply with the mandatory allocation referred to above whether partial or full, will be slapped a penalty of at least PHP 500,000.00. However, this was removed from the *Magna Carta for MSMEs* in 2008, which simply mandated that the *Bangko Sentral ng Pilipinas* (the “BSP”) to formulate rules for the effective implementation of the mandatory allocation provision.⁷⁰

Pursuant to this mandate, the BSP issued *Bangko Sentral Circular* 625 s. 2008, which penalized noncompliance with a graduated fine ranging from PHP 180.00 to PHP 500,000.00. This effectively weakened the force of the law to obligate banks to provide credit to SMEs. Once they calculate that the cost of violation would be lower than the potential cost of SME-borrower default, they can opt to pay the fines to be imposed.

They may be the reason why, as noted by Mr. Benel Lagua, Executive Vice President and Chief Development Officer of the Development Bank of the Philippines and Chief Executive Officer of the Industrial Guarantee and Loan Fund, the overall compliance of the banking sector with the Mandatory Credit under the *Magna Carta for MSMEs* is only 5.34 percent for micro/small and 6.07 percent for medium (2012).⁷¹ He also

68 Ibid., Sec. 14, as amended by Republic Act 9501.

69 Ibid., Sec. 15, as amended by Republic Act 9501.

70 Ibid., Sec. 15, as amended by Republic Act 9501.

71 Lagua, Benel (2013). “How Do We Reinvent and Innovate Access to Finance for SMEs?” Presentation

mentioned that while the banking sector loan portfolio increased by 154.9 percent from 2001 to 2012, the micro/small loan portfolio increased by 30.05 percent, and the medium loan portfolio increased by 143.75 percent.⁷² Out of the 19 Universal Banks, 14 did not comply in Micro & Small Enterprise Portfolio and 6 in the Medium Enterprise Portfolio.⁷³

Mr. Laguna also notes that “MSMEs only get one-fifth financing of what large enterprises are getting.”⁷⁴ He also noted the unmet demand in various studies: (1) Scoping Study in 2006, USD 2.5 billion; (2) Philexport, PHP 67 billion; (3) Nangia and Villar (2006), PHP 76-270 billion; and (4) Aldaba, PHP 130 billion.⁷⁵

- Other incentives granted to Barangay Micro Business Enterprises. Republic Act 9178 (2002), otherwise known as the Barangay Micro Business Enterprises Act of 2002 (the “BMBE Law”), provides certain incentives to microenterprises, that is, enterprises “engaged in the production, processing, or manufacturing of products or commodities x x x” with total assets, excluding the land where office, plant, and equipment of the enterprise, amounting to not more than Three Million Pesos (PHP 3,000,000.00).⁷⁶ These benefits are as follows:
 - a. Income tax exemptions and lower or exemption from local taxes, fees, and charges at the discretion of the local government units (LGUs);⁷⁷
 - b. Exemption from the coverage of the Minimum Wage Law;⁷⁸
 - c. Special credit window to be set up by the Land Bank of the Philippines (LBP), the Development Bank of the Philippines (DBP), the SB Corporation, the People’s Credit and Finance Corporation, the Government Service Insurance System (GSIS), and the Social Security System (SSS);⁷⁹

at the Roundtable Discussion on Priming Philippine SMEs for the 2015 ASEAN Integration held at UP Institute for Small-Scale Industries, Diliman, Quezon City on 13 August 2013 accessed at <http://issi.upd.edu.ph/PJIE.pdf>.

72 Ibid.

73 Ibid.

74 Ibid. Laguna, Benel (2013). “How Do We Reinvent and Innovate Access to Finance for SMEs?” Presentation at the Roundtable Discussion on Priming Philippine SMEs for the 2015 ASEAN Integration held at UP Institute for Small-Scale Industries, Diliman, Quezon City on 13 August 2013 accessed at <http://www.entrepreneurship.org.ph>.

75 Ibid.

76 Republic Act 9178, Sec. 3(a).

77 Ibid., Sec. 7.

78 Ibid., Sec. 8.

79 Ibid., Sec. 9, par. 1.

- d. Creation of a special guarantee window to guarantee the loans granted to microenterprises to be established by the SB Corporation and the Quedan and Rural Credit Guarantee Corporation (QUEDANCOR);⁸⁰
- e. BMBE Development Fund for technology transfer, production, and management training and marketing assistance to SMEs. The BMBE Development may be accessed by the Department of Trade and Industry (DTI), the Department of Science and Technology (DOST), the University of the Philippines Institute for Small Scale Industries (UP ISSI), Cooperative Development Authority (CDA), Technical Education and Skills Development Authority (TESDA), and the Technology Livelihood Resource Center.⁸¹

2. Challenges to Ease of Doing Business

It goes without saying that ease of doing business helps SMEs thrive in a competitive environment more so than the already established large enterprises. The lack of it can make or break a fledgling enterprise, becoming prohibitive and a disincentive.

Various Ease of Doing Business Surveys

Various competitiveness indicators on ease of doing business show the Philippines to be lagging behind its other Asian neighbors. Through the years, the Philippines either improved, regressed, or remained the same (the blank spaces indicate no changes from the previous year) as the previous year in the following indicators on ease of doing business (see Table 5).

Note that the following indicators had no movement at all: getting electricity, registering property, protecting investors, and enforcing contracts.

While the Philippines has made substantial improvements in streamlining its regulatory processes that affect enterprises' startup and operations, it appears that the country continues to lag behind several neighbors in providing an enabling bureaucracy for businesses.

a. IFC Doing Business Reports

Five survey-based reports have detailed bottlenecks as well as reforms in an attempt to characterize Philippine and Asian firms' daily experience with securing various permits and licenses. One of these, the annual Doing Business report by the International Finance Corporation (IFC) of the World Bank Group provides what is perhaps the

⁸⁰ Ibid., Sec. 9, par. 4.

⁸¹ Ibid., Sec. 10.

Table 5. Ease of Doing Business Indicators

Indicators	2008	2009	2010	2011	2012	2014
Starting a Business	Regressed			Improved		
Dealing with Construction Permits				Regressed		Improved
Getting Electricity						
Registering Property						
Getting Credit			Improved			Improved
Protecting Investors						
Paying Taxes			Improved			Improved
Trading across Borders		Improved		Improved		
Enforcing Contracts						
Resolving Insolvency			Improved		Improved	

Source: Business Reforms in the Philippines, <http://www.doingbusiness.org/reforms/overview/economy/philippines>.

most comprehensive picture of regulatory regimes not just in the Philippines but in hundreds of other countries. In its Doing Business Report (2014), the Philippines was deemed among the ten most improved in the world after it rose 25 spots from 133rd in 2013 to rank 108th in 2014 out of 189 economies.⁸²

The Philippines is in the middle third of the global rankings and is behind five Southeast Asian neighbors (Singapore, Malaysia, Thailand, Brunei, and Vietnam). The Doing Business Report noted government initiatives to cut down on the number of certain documentary requirements, establish electronic filing systems, and provide access to credit information, as well as ratify the Data Privacy Act and the Financial Rehabilitation and Insolvency Act.

⁸² World Bank Group, Doing Business 2014. Available at <http://www.doingbusiness.org/~media/GIAWB/Doing%20Business/Documents/Annual-Reports/English/DB14-Full-Report.pdf>. Accessed April 15, 2014.

Table 6. Philippines – Doing Business 2014

TOPICS	DB 2014 Rank	DB 2013 Rank	Change in Rank	Position in Rankings
Starting a Business	170	166	-4	bottom third
Construction Permits	99	95	-4	middle third
Getting Electricity	33	33	no change	top third
Registering Property	121	119	-2	middle third
Getting Credit	86	126	+40	middle third
Protecting Investors	128	127	-1	bottom third
Paying Taxes	131	144	+13	bottom third
Trading Across Borders	42	41	-1	top third
Enforcing Contracts	114	112	-2	middle third
Resolving Insolvency	100	164	+64	middle third

Source: World Bank.

The latter law provides a legal framework for out-of-court settlements in times of insolvency as well as lets creditors' committees have a say in proceedings. Nevertheless, the country failed to keep up with improvements by other countries and thus saw its rankings in seven out of ten indicators deteriorate, while only two improved and one remained unchanged.

Worst performing indicators

As shown above, starting a business and paying taxes are the indicators where the Philippines ranks bottom third in the world. It takes 15 procedures to register a business in the country compared to an East Asia & Pacific average of and the OECD average of 5. Furthermore, it takes 35 days to register a business in the Philippines and the cost is worth 18.7 percent of income per capita.

In terms of paying taxes, businesses in the Philippines have to deal with 36 payments in a year, compared to just an average of 25 in the East Asia & Pacific and an average of 12 among OECD members. This entails roughly 193 hours per year according to local accounting firms. On top of that, the total tax rate is estimated to make up 44.5 percent of profit, compared to the 34.5 percent regional average and 41.3 percent OECD average. Be that as it may, the report noted the efforts to introduce electronic system for tax filing and payment of social security contributions.

Best performing indicators

The country fares best in the indicator dealing with ease of trading across borders, which is particularly important if enterprises are to participate in and take advantage

of economic integration. The Philippines is ranked among the top third in this respect, as it takes only 6 documents to export and 15 days to process outbound shipments, both of which are roughly comparable to the OECD average. Furthermore, the export cost per container is roughly half of the OECD cost. The experience is relatively the same in terms of import processes.

The annual Doing Business Report collected data on processing times and costs from each economy's largest city, with Quezon City representing the Philippines. For 2011, however, the report provided a more detailed look into the country's 21 cities to emphasize the important role the local government plays besides efforts from the national government. The report found that no single city does equally well on all three indicators of starting a business, registering property, and obtaining construction permits. It explained that the variation is due to the involvement of local government units in business startup and construction permit requirements.⁸³ However, the 2011 report noted that "Philippine cities actively reformed their business regulations over the past two years," and that the improvements generally stemmed from "re-engineering business processes rather than amending laws."⁸⁴ Examples cited include Davao City's single assessment of business permit fees in a centralized office, lifting of a rule in Pasay City requiring businesses to apply for a separate zoning clearance and electrical permit rather than just submitting the building owner's permits, and the nationwide land-titling computerization project of the Land Registration Authority.

b. 2009 Enterprise Survey by the World Bank

The second survey-based report similarly tracking red tape is the 2009 Enterprise Survey also by the World Bank.⁸⁵ Unlike the Doing Business Report, which uses time and cost estimates from accountants and lawyers who do the processing on behalf of different sized firms, the Enterprise Survey is able to differentiate the responses of small- and medium-sized firms from the larger respondents and also appears to place the Philippines at par with its neighbors. The report is based on interviews with 1,326 firms across the National Capital Region, Calabarzon, Metro Cebu, and Central Luzon from May through December of 2009. 419 firms of these firms were small enterprises and 570 were medium-sized enterprises.

The survey found that 6.6 percent of small firms and 15.5 percent of medium-sized firms in the Philippines expect to give a gift to obtain an operating license, which is comparable to the average response among East Asia & Pacific firms. Respondents were also more upbeat than their regional counterparts in terms of the length of time expected to obtain an operating license, with small- and medium-sized firms claiming it takes roughly 10 days instead of 15 reported by their Asian peers.

83 World Bank Group, *Doing Business in the Philippines 2011*. Available at <http://www.doingbusiness.org/~media/GIAWB/Doing%20Business/Documents/Subnational-Reports/DB11-Sub-Philippines.pdf>. Accessed 15 April 2014.

84 Ibid.

85 World Bank Group, *Enterprise Surveys – Philippines Country Profile 2009*. Available at <http://www.enterprisesurveys.org/~media/FPDKM/EnterpriseSurveys/Documents/Profiles/English/Philippines-2009>. Accessed 15 April 2014.

Based on questions covering other areas besides starting up, the report states that the top constraints commonly cited by Philippine firms are practices of the informal sector, access to finance, tax rates, electricity, political instability, business licenses and permits, corruption, crime, theft, and disorder, customs and trade regulations, and an inadequately educated workforce.

c. Philippine Institute for Development Studies Report

A third report from the Philippine Institute for Development Studies provides an added dimension by showing how top concerns of SMEs in the manufacturing sector change depending on whether the company is part of an international production network (IPN) or not. It appears that IPN firms feel less exposed to or are less concerned with business regulations than non-IPN firms. The report states that “IPN firms are primarily concerned with product and price barriers and difficulties in establishing and maintaining trust with business partners, while non-IPN firms’ major concerns are tax, tariff and nontariff barriers and the country’s deteriorating business environment.”⁸⁶

The report was based on a survey administered in late-2009, which drew responses from 101 manufacturing firms. The same enterprises were asked to rank the assistance they need the most to overcome barriers to doing business. For IPN firms, they called for financing assistance. For non-IPN firms, the most crucial assistance cited was technology information.

d. Global Enabling Trade Report by the World Economic Forum

Similarly recognizing the importance of global exposure to firms’ prospects for growth, the latest Global Enabling Trade Report by the World Economic Forum focuses on regimes of economies in terms of ease of crossing borders. In the 2012 report, the Philippines rose 20 spots to 72nd out of 132 economies from the last ranking issued in 2010.⁸⁷ This puts the Philippines in the middle third of the list and lagging behind five ASEAN countries: Singapore, Malaysia, Thailand, Indonesia, and Vietnam.

While the Philippines does especially well in the indicator of market access (14th out of 132 economies) because of its low tariffs, it fares worse in terms of border administration (72nd), transport and communications infrastructure (91st), and business environment such as regulatory environment and physical security (107th).

Another report similarly focusing on trade facilitation went beyond indicators of processing times and costs. Using two surveys, the report found that ASEAN firms have been commonly and significantly hobbled by “unofficial facilitation fees, tedious

86 Erlinda Medalla, Rafaelita Aldaba, Fatima del Prado & Donald Yasay. Integrating SMEs into the East Asian Region: Philippines. Philippine Institute for Development Studies Discussion Paper. 2 (2010).

87 World Economic Forum, Global Enabling Trade Report 2012. Available at <http://www.weforum.org/reports/global-enabling-trade-report-2012>. Accessed 23 March 2014.

goods declaration, poor information on procedures, difficult release of goods, and complex refund and appeals process”⁸⁸ at the border. As such, one of the paper’s conclusions is that top ranked barriers are those that can be “remedied through administrative decisions within the Customs agency.”⁸⁹

e. Other Relevant Studies

The foregoing reports show how red tape is a common problem shared by countries in the region to varying degrees. They further show how the Philippines has made some strides in improving the ease of startup and operations for enterprises; however, the country has yet to catch up with the more supportive business environments of its neighbors.

Cognizant of the constraints posed by cumbersome business regulations in the Philippines, these survey-based reports have prescribed various ways to move forward. Benchmarking, which was accomplished by the survey-based rankings discussed in the previous section, is already a step in the right direction.

According to a working paper from the Asian Development Bank, comparative benchmarking allows governments to understand why other countries may be doing better as well as highlights where further efforts are needed. It argues that benchmarking can “(i) provide important incentive structures that encourage the sharing and implementation of good practices through peer pressure mechanisms and (ii) serve as a starting point for dialogue between government and the private sector on reform priorities.”⁹⁰

Focusing on the Philippines, another report meanwhile synthesizes various competitiveness rankings to support its conclusion that major constraints to private sector growth “continue to be inadequate infrastructure, corruption, cumbersome business procedures, poor tax and customs administration, barriers to market entry and competition, weak property rights, high energy costs, and lack of equitable and effective regulation and enforcement.”⁹¹ As such, it recommends a 12-point action plan, saying the Philippines should:

- adopt legislation on freedom of information;
- intensify implementation of anti-red-tape legislation;
- institutionalize and capacitate the function of regulatory impact analyses;

88 de Dios, Loreli de Dios, *Business Views on Trade Facilitation*, ERIA Discussion Paper 1 (2009).

89 Ibid.

90 Schou-Zibell, Lotte and Srinivasa Madhur (2010). *Regulatory Reforms for Improving the Business Environment in Selected Asian Economies—How Monitoring and Comparative Benchmarking Can Provide Incentive for Reform*, ADB Working Paper Series on Regional Economic Integration, Abstract.

91 Haydarov, Aziz (2011). *Philippines: Private Sector Development. Challenges and Possible Ways to Go*, Southeast Asia Working Paper Series. v.

- improve coordination with local government units (LGUs) during preparation of investment projects and streamline national legislation and the Local Government Code;
- update labor legislation and improve the minimum wage determination system;
- adopt and institutionalize an antimonopoly framework;
- institutionalize the judiciary-business link and streamline the mechanism for implementation of arbitration awards;
- reduce the number of business registration procedures and fully operationalize the Philippines Business Registry;
- simplify taxation of small businesses (including considering exempting small businesses from income taxes during the first three years of operation);
- operationalize financial rehabilitation and insolvency legislation;
- complete cadastral titling of land and establish a central registry for land titles; and
- strengthen the National Competitiveness Council to become the main public-private mechanism for PSD policy coordination and consultation.⁹²

The PIDS paper that focuses on integrating SMEs into the global supply chain, for its part, states that besides equipping enterprises with the knowhow and links to participate in production networks, the government must also “create an enabling environment for firms to survive and realize their potentials.”⁹³ Otherwise, it stated, corruption and excessive bureaucracy will remain a constraint to doing business in the Philippines.

Analysis and Implications to Philippine SME Internationalization

The findings of the doing business surveys above reflect the successes gained by the government in its efforts to streamline business registrations. The SMED Plan 2004-2010 and MSMED Plan 2011-2016 reflect the overall government effort to streamline these registrations. The results of these efforts are noted particularly in the IFC Doing Business Report 2014 findings that cities reformed their business registration processes over the past two years.

These efforts, however, confirm the assessment of this paper that the focus of government resources has been in improving the readiness of SMEs to start and operate a business in the Philippines, and less in preparing them to compete and participate in the global marketplace. For example, a number of studies reviewed above indicate

⁹² Haydarov: vi-vii.

⁹³ Medalla, Erlinda, Rafaelita Aldaba, Fatima del Prado & Donald Yasay (2010). Integrating SMEs into the East Asian Region: Philippines. Philippine Institute for Development Studies Discussion Paper. 26.

that customs and trade regulations and corruption at the border pose challenges to ease of doing business in the Philippines, while constraints in starting a business has somewhat eased.

It is also notable that in the PIDS study noted above, companies that are part of international production networks (IPN) are more concerned about product and price barriers and difficulties in establishing and maintaining trust with business partners, while non-IPN members are concerned about tax, tariff and nontariff barriers and the country's deteriorating business environment.

This is another example of a need to make a distinction among SMEs beyond such indicators as total assets and number of employees. It also emphasizes the need to identify specific SME concerns to ensure the effectiveness of targeted policies and strategies.

What is clear though from the studies and surveys reviewed above is that there is need to rationalize laws and regulations that support policies and strategies for upgrading and engaging in higher value activities that will prepare SMEs to engage in the global market place.

Challenges to upgrading and higher value activities will be discussed in more detail in Part III below.

Part 3. Upgrading and Higher Value Activities

Likened to the Olympics, participating in the global market requires much. Liberal (2001) noted that the global market is "participated in by countries with different endowments in natural resources, cultural orientation, and values, and levels of economic development including political environment."⁹⁴ Indeed, some are better equipped and better prepared; there is no leveling of playing field; only the fit survive.⁹⁵

Edgar Rodriguez (2000) made a study of the survival rates of manufacturing enterprises from 1990–1995 and found that more than half of the 5,330 firms registered in 1990 disappeared in 1995 (small firms obtained the lowest survival rate of 19 percent, followed by medium firms with 23 percent and finally by large enterprises with 35 percent while microenterprises posted a rate of 48 percent).⁹⁶

A more in-depth study was made by Dr. Aimee Hampel-Milagrosa⁹⁷ (2013). Using the concept of upgrading to mean (1) increase in income, productivity, and number of

94 Liberal, Arlene Eleanor E. (2001). 'Ay There's the Rub': Taking a Leaf from SME Experience. Bridging the Gap: Philippine SMEs and Globalization, Oscar M. Alfonso, ed., Quezon City, Philippines: SERDEF and UP ISSI.

95 Ibid.

96 Rodriguez, Edgar (2000). Productivity and Dynamics of Philippine Manufacturing SMEs in the New Economy (unpublished).

97 Hampel-Milagrosa, Aimee (2013). Micro and Small Enterprise Upgrading in the Philippines: The

paid-in workers; (2) transition from informal to formal; and (3) firm-level innovation, she defined enterprise upgrading as “a growth through innovation” hence “upgraders” are considered as “the handful of exceptional entrepreneurs whose enterprises managed to progress from micro and small into medium sized enterprises during a specific period of time through the introduction of various innovation.”

Looking at four critical success factors to upgrading, i.e., the entrepreneur, the enterprise, the networks, and the business environment, Hampel-Milagrosa (2013) concluded that upgrading occurs through different trajectories although most rely on entrepreneurial characteristics. This study noted that a lot of upgraders used different strategies and debunked the idea that creation of enabling business environments alone guarantees enterprise upgrading.

This study generated insights on enterprise upgrading in many senses. It showed that (1) entrepreneurs use a combination of strategies (both in substitution and complementation) to increase innovation, ensure survival, and upgrade their enterprises; (2) entrepreneurs have to simultaneously overcome structural and sector-specific constraints in order to upgrade; (3) there are intangible entrepreneur characteristics that influence upgrading potential; (4) the importance of personal and professional networks in enterprise upgrading could not be discounted; (5) conflicting industrial development and international trade policies make it extremely difficult for enterprises to upgrade; (6) enterprise growth and upgrading is possible in “dying” sectors but requires a complete overhaul of strategic approach at all levels. The research concluded with policy recommendations for interventions geared toward each level of the onion model, with the ultimate objective of increasing Philippine micro and small enterprises’ upgrading potential.

A. Government Efforts in Providing Upgrading Assistance and Support for Engaging in Value Added Activities

Upgrading assistance in the Philippines is provided primarily by the DTI and four attached agencies: (1) the Industry and Investments Group (IIG), (2) the International Trade Group (ITG), (3) the Consumer Welfare and Trade Regulation Group (CWTRG), and, (4) the Regional Operations and Development Group (RODG).

In terms of business development, the RODG is crucial. It has many program and services that cater to developing businesses namely, (1) the Export Pathways Program (EPP), (2) the National Economic Research and Business Assistance Center (NERBAC) or a one-stop center for would-be entrepreneurs in business registration, knowledge management, and investment promotion and facilitation, (3) the MSME Development Plan Localization involving the various local government units (LGUs), and (4) the National Industry Cluster Capacity Enhancement Project (NICCEP). The NICCEP

aims to enhance the capacity of industry clusters with the shared services facilities, agricultural support projects, traceability for agri-fishery products with international standards and regulations, rural microenterprise promotion, small and medium enterprise development program.

Cognizant of the challenges to SMEs in engaging in higher value activities, relevant government agencies have prepared several studies and master plans to improve their innovation capacity.

The Philippine Export Development Plan 2011-2013, meanwhile, lists the need to move up the value chain as among its three core product strategies, and it aims to accomplish this by securing foreign and local investments that are more involved in the production of finished goods and services as well as higher-value activities.⁹⁸ The plan goes on to break down strategies by sector, for instance, listing improved funding of government laboratories needed by food exporters, coordinating agencies for garments skills training, and marketing Philippine knowledge industries for the business process outsourcing sector, among others.⁹⁹

In 2007, the Department of Science and Technology (DOST) also spearheaded the “FILIPINNOVATION” project. It lays down the National Innovation Strategy, which was crafted through the concerted effort of government agencies, academe, and business enterprises. It calls for action in four areas: (a) strengthening Filipino human capital, (b) supporting business incubation and acceleration efforts, (c) regenerating the policy environment for innovation, and finally (d) upgrading the Filipino mindset toward a culture of innovation.¹⁰⁰

In line with this, the 2009 Survey of Innovation Activities was completed involving 474 establishments across the country in order to inform policy making by determining factors that drive innovation among firms. The study found that engagement in knowledge management practices and growing the company’s size were among the major determinants of innovative behavior while cost factors, limited government support, and weak knowledge networks were identified as barriers.¹⁰¹ As such, the study recommends a policy framework tailored to growing SMEs as well as fostering knowledge sharing across academe, the public sector, and private enterprises. It also notes firms’ demands for technical support and training, tax rebates and infrastructure support.¹⁰²

98 Department of Trade and Industry, Philippine Export Development Plan 2011-2013 21 (2011).

99 Ibid., 21, 39 (2011).

100 Department of Science and Technology. FILIPINNOVATION. Available at <http://www.filipinnovation.dost.gov.ph/aboutus.htm>. Accessed 8 November 2013.

101 Albert, Jose Ramon G., Rafaelita M. Aldaba, Francis Mark Quimba, and Donald Yasay (2011). Results of the 2009 Survey of Innovation Activities (SIA), 2011-15 Philippine Institute for Development Studies Discussion Paper Series: 39.

102 Ibid., 22.

Under the FILIPINNOVATION strategy, the DOST reports that several programs have been launched to encourage firms to use or develop new techniques and technologies.¹⁰³ An Engineering Research and Development for Technology consortium was established among seven schools, which offered engineering scholarships for masters and doctoral students through the support of government in a bid to produce research in the areas of energy, environment, infrastructure, ICT, semiconductor and electronics, and agriculture.¹⁰⁴ Another program, meanwhile, was tasked with delivering market intelligence to firms in the agriculture and fisheries industries. The DOST and Philippine Economic Zone Authority (PEZA) also established a DOST-PEZA incubation program to support ICT startups. These efforts jibe with concerns raised in the abovementioned master plans over technical skills upgrading and knowledge sharing.

In addition, the DOST also manages the Small Enterprise Technology Upgrading Program (SET-UP), which provides technical assistance, laboratory and equipment rental, product testing and packaging services, and networking assistance to SMEs in a bid to improve their productivity and efficiency. Under this initiative, for instance, the government has helped firms in the metal industry to acquire machines and tools and also improve food packaging and processing of companies in the food sector.¹⁰⁵ This initiative thus responds to SMEs demands for support in defraying innovation costs. From 2006 to 2009, the program is reported to have assisted 4,394 firms that needed technology transfer and commercialization and also conducted over 4,158 technology trainings for over 12,000 firms.¹⁰⁶

The DTI's Philippine Trade Training Center, for its part, provides training programs and instructional materials for SMEs on topics that include innovation strategies, laboratory auditing, and computer literacy.¹⁰⁷

The Board of Investments' annually issued Investment Priorities Plan (IPP) lists enterprises engaged in research and development as among those qualified for a package of fiscal and nonfiscal incentives which include income tax holidays of up to eight years and exemption from taxes on exports, breeding stocks, and genetic materials as provided by The Omnibus Investments Code of 1987.¹⁰⁸ This provision covers "all R&D activities" including research and testing laboratories, incubation centers, common service facilities, establishments that aim to develop competencies in entrepreneurship and R&D, and training and learning institutions.¹⁰⁹ This thus

103 Department of Science and Technology. Programs Launched. Available at <http://www.filipinnovation.dost.gov.ph/programlaunched.htm>. Accessed 8 November 2013.

104 Ibid.

105 Department of Science and Technology. SET UP. Available at <http://webgis.dost.gov.ph/>. Accessed 8 November 2013.

106 MSMED Plan 2011-2016: 68 (2010).

107 Philippine Trade Training Center (2012). Annual Report 2012.

108 Memorandum Order No. 40 (13 June 2012).

109 Board of Investments. 2012 Investments Priorities Plan. 41 (2012).

addresses demands of firms made known in the Survey of Innovation Activities for tax rebates and support in bringing down innovation costs.

However, despite these efforts, there is general agreement that SMEs in the Philippines lag behind those in other countries when it comes to producing goods and engaging in activities that are of high value.

The local SME sector contributed only 35.7 percent of total value-added in the economy in 2006 even as it accounted for 99.6 percent of the number of total establishments in the country.¹¹⁰ The DTI, furthermore, has pointed to the SME's sector's "low productivity due to lack of access to new technology, weak technological capabilities, and failure to engage in innovation and research and development activities."¹¹¹

This dearth in innovation is reflected in the type of industry SMEs typically engaged in—47 percent of the 816,759 SMEs recorded in 2011 were in the wholesale and retail trade business, which is not generally considered as a high value-added activity, while only 10.5 percent were in professional, scientific, technical, education and information and communication-related industries.¹¹²

Moreover, the state-run think tank Philippine Institute for Development Studies (PIDS) has similarly noted that unlike South Korea, Singapore, and Taiwan, the Philippines still has a long way to go in terms of upgrading technology, developing human resources, and sharpening specialized skills among small and medium enterprises.¹¹³ Based on a survey of four respondents in the SME sector, the PIDS study concluded that efforts to implement SME technology upgrading and innovation transfer had "little to no concrete impacts."¹¹⁴

Part 4. Assessment and Policy Recommendations

In addition to the operational constraints¹¹⁵ already identified in numerous studies, this study highlighted constraints in SME development policy making, the existing institutional framework, regulatory blocks and little or no discernible impacts of efforts to assist SMEs upgrade and engage in high-value activities.

The findings of the study are summarized as follows:

1. Characteristics of Philippine SMEs

- a. Limited capacity to grow and compete due to such operational constraints as lack of access to finance, information, relevant

110 MSMED Plan 2011-2016:10 (2010).

111 Ibid., ii (2010).

112 Department of Trade and Industry, Micro, Small and Medium Enterprises (MSMEs). Available at <http://www.dti.gov.ph/dti/index.php?p=321>. Accessed 8 November 2013.

113 Aldaba, Rafaelita M. ASEAN Economic Community 2015 SME Development: Narrowing Development Gap Measure (2013). 2013-05 Philippine Institute for Development Studies Discussion Paper Series:15.

114 Aldaba: 14.

115 Such as lack of access to finance, information, relevant technologies, limited marketing skills and management capacity, high business costs and limited attention to research and development.

technologies, limited marketing skills and management capacity, high business costs, and little attention to research and development

- Hence, most SMEs are micro and engaged in simple trading and service activities
- b. Disconnect between opportunities from international trade and SME awareness of these opportunities and capacity to maximize them
- c. Unsupportive domestic regulatory environment
- d. Risk averseness of Philippine SMEs due to limited exposure to competition and skills development

2. Aspects of SME Development

a. Policy Development and Implementation

- Current databases are not sufficient to provide a meaningful profile of Philippine SMEs that would facilitate their effective definition and characterization as a means of providing relevant information for targeted policies and strategies.
- Initiatives of government agencies responsible for implementing the SME development plans are skewed toward “readiness” issues, such as streamlining business registrations, supporting startups, and clustering initiatives through the One-Town-One-Product program that emphasize production of food and agricultural products.
- No clear policy framework or strategy for Philippine SME internationalization.

b. Institutional Development

- Implementation of the Magna Carta for MSMEs is dispersed among various government agencies that act on an ad hoc basis.
- Weak implementation of programs and activities under the SME development plans due to poor coordination among implementing agencies.

c. Legal and Regulatory Environment

- Limited access to government information
- Red tape
- Lack of coordination among LGUs during preparation of investment projects
- Disconnect between national legislations and the Local Government Code
- Unresponsive labor laws to market realities
- Ineffective antimonopoly laws

- Disconnect between business realities and judicial decisions
- Cumbersome business registration procedures and incomplete Philippine Business Registry
- Cumbersome taxes on small businesses
- Inadequate implementation of financial rehabilitation and insolvency legislation
- Incomplete cadastral titling of land
- No mechanism for private sector development policy coordination and consultation.

3. Upgrading and Higher Value Activities

- a. Low survival rate of enterprises, such as manufacturing enterprises
- b. Characteristics of upgrading entrepreneurs
 - Entrepreneurs use a combination of strategies to increase innovation, ensure survival, and upgrade enterprises
 - Entrepreneurs have to simultaneously overcome structural and sector-specific constraints in order to upgrade
 - There are intangible entrepreneur characteristics that influence upgrading potential
 - The importance of personal and professional networks in enterprise upgrading could not be discounted
 - Conflicting industrial development and international trade policies make it extremely difficult for enterprises to upgrade
 - Enterprise growth and upgrading is possible in “dying” sectors but require a complete overhaul of strategic approach at all levels
- c. Little or no impact of government upgrading and innovation policies to SMEs

Policy Recommendations

To address the above findings, this paper proposes the following recommendations:

A. Assess Current Databases and Data Gathering Capabilities

- Review the Philippines’ definition of SMEs, its data-gathering capabilities, assess the usefulness of existing data for effective policymaking, monitoring, and evaluation, and identify specific actions moving forward to address existing constraints. Ensuring the reliability of data used for policymaking and consistency of definitions is the first step toward identifying targeted strategies and interventions to support SME growth and internationalization.

B. Distinguish SME Internationalization Policies from General SME Development Policies

- Link SME development policies to related trade, industrial, and development policies to coordinate government policies that promote the internationalization of domestic enterprises.
- Adopt longer-term development plans with clear development approaches, benchmarks, and periodic monitoring and evaluation.
- Identify relevant APEC and other regional initiatives that will be most useful to the Philippines in achieving its SME internationalization goals.

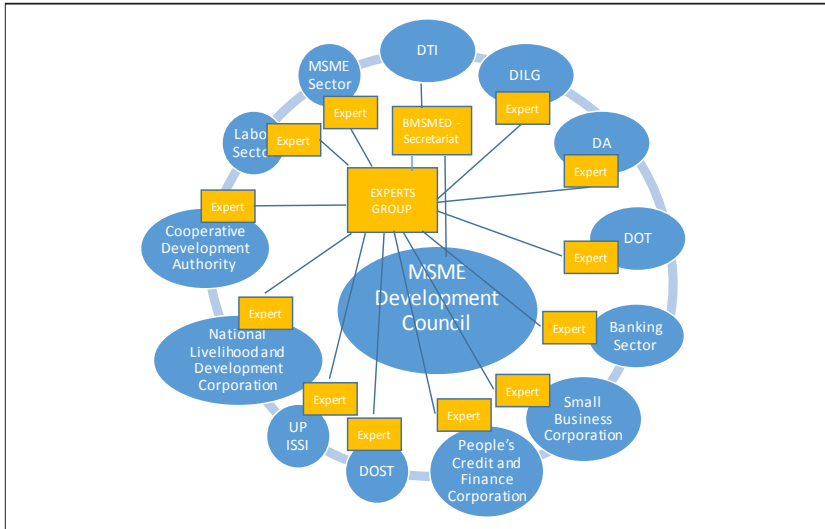
C. Rethink the Role of the MSMED Council and the Organizational Structure of Implementing Agencies

- Strengthen the mandate of the SME development agency
 - Consider amending the present Magna Carta for MSMEs to strengthen the mandate of the MSMED Council or other agency so that it can acquire and maintain specialized skills in SME development.
 - Instead of having representatives of various agencies and LGUs as members of the agency or implementors of the Magna Carta for MSMEs (as is the case with the MSMED Council), the SME agency will have resident representatives in the various agencies and LGUs.
 - These representatives will be responsible for tracking the various programs and activities in these agencies and identifying which of these can be adopted into the overall SME development effort.
 - These representatives should thus be technically skilled career personnel whose main purpose is to assist in building a coherent effort to achieve an established long term policy and strategy for SME growth and internationalization.
 - Establish strong linkages with similar bodies in the various APEC economies to build technical capacity, share best practices in SME internationalization and provide relevant market information to various economies.

D. Identify Specific and Targeted Strategies That Will Facilitate Upgrading and High Value Activities for SME Internationalization

- Work with APEC and other regional groupings to establish a system of benchmarking each country's progress in SME development
According to a working paper from the Asian Development Bank, comparative benchmarking allows governments to understand why other countries may be doing better. It also highlights where further

Fig. 6. Proposed Organizational Structure



Source: Unpublished manuscript of Joan P. Serrano

efforts are needed. The working paper notes that benchmarking can “(i) provide important incentive structures that encourage the sharing and implementation of good practices through peer pressure mechanisms and (ii) serve as a starting point for dialogue between government and the private sector on reform priorities.”¹¹⁶

- Formulate a coherent industrial clustering strategy

Extent of Government Intervention in Encouraging the Growth of Clusters

There is disagreement over the extent of government intervention that is necessary and effective for realizing gains from SME clustering and participation in global production networks. Some contend that government action and institutions are central to supporting SMEs. Dhungana of the United Nations Economic and Social Commission for Asia and the Pacific, in writing about strengthening the competitiveness of small enterprises amid globalization, had stated that “national governments would have a responsibility to formulate and implement policies to adjust their economies smoothly and efficiently to benefit from the globalization process, especially if SMEs are to be promoted and sustained in this new economic environment”.¹¹⁷

116 Schou-Zibell, Lotte and Srinivasa Madhur (2010). Regulatory Reforms for Improving the Business Environment in Selected Asian Economies—How Monitoring and Comparative Benchmarking Can Provide Incentive for Reform, ADB Working Paper Series on Regional Economic Integration, Abstract.

117 Dhungana, Bhavani P. (2003). Strengthening the competitiveness of small and medium enterprises

Henderson et al. similarly argue that institutional arrangements “can be of considerable importance” in determining how well global production networks (“GPNs”) create value.¹¹⁸ Governance, they said, is critical for regulating working conditions and ensuring sustainability of economic development derived from the integration of enterprises.

Others, meanwhile, contend that government intervention should be limited so as not to crowd out indigenous activity and support mechanisms that often arises from the clusters themselves. Ernst and Kim, for instance, have focused their prescriptions on how enterprises can govern themselves. Lead firms or so-called global flagships should encourage knowledge transfer to local suppliers to enhance their capabilities, strengthen the network’s competitiveness, and also ensure supplier loyalty.¹¹⁹ Local suppliers, for their part, should be proactive in exploiting benefits from the network by upgrading their absorptive capacity, developing and retaining their human resources, and also transferring knowledge to lower-tier suppliers.¹²⁰

Carrie, for his part, has lauded the Arizona state government’s approach of “not imposing any particular way of working on the clusters” and instead limits policy intervention to merely “giving assistance and encouragement to the players in an industry to get together.”¹²¹ Another case study, this time focusing on the Torreon blue jean cluster in Mexico, claims that support from institutions like the government and trade associations were not central to the sector’s development there and it was instead the arrival of a new type of US buyer that prodded firms to upgrade capabilities in order to offer full-package apparel production.¹²²

Tailor-Fitting Cluster Development Policies

It appears that the middle ground is for government policy to be tailored to the realities of the market and the type of cluster observed.

Van Dijk and Sverrisson recommend that for clusters still in the initial stages of development, “space should be reserved for smaller units in

in the globalization process: prospects and challenges. *Investment Promotion and Enterprise Development Bulletin for Asia and the Pacific* No. 1:1.

118 Henderson, Jeffrey, Peter Dicken, Martin Hess, Neil Coe, and Henry Wai-Chung Yeung. (2011). *Global production networks and the analysis of economic development*. 9-3 Review of international political economy : 455.

119 Ernst, Dieter and Linsu Kim. (2002). *Global production networks, knowledge diffusion, and local capability formation*. 31-8 Research policy: 38.

120 Ernst et al.: 38.

121 Carrie, Allan S. (2000). *From integrated enterprises to regional clusters: the changing basis of competition*. 42-2 Computers in Industry: 292.

122 Bair, Jennifer & Gary Gereffi. (2001). *Local clusters in global chains: the causes and consequences of export dynamism in Torreon’s blue jeans industry*. 29-11 World development:1889.

existing industrial zones, where cooperative competition would be possible.”¹²³ Support for clusters in advanced stages of development, meanwhile, should be concentrated in lifting barriers on technology transfer like import restrictions on equipment. Governments would also do well to encourage the formation of associations as well as formalize regular interaction with government agencies. These are said to help prepare clusters for when the country moves into creating links with foreign markets for larger opportunities.

Knorringa and Meyer-Stamer similarly recommend approaches to encouraging the formation of industrial districts—what they had described to be the most evolved type of cluster—that are tailor fitted to characteristics of the cluster. For clusters with little cooperation among enterprises to begin with, the authors report that the introduction of large firms that outsource parts of their production process as well as the institutionalization of information exchange through business associations have been helpful based on case studies.¹²⁴

Meanwhile, for cooperative clusters faced with adjustment pressures such as shocks from export market regulations or from economic crises, case studies have shown that government has not been central to helping firms cope and it was instead the business associations that provided valuable support.¹²⁵ In these circumstances, governments are advised to intervene only by providing infrastructure, financing, and stable regulation frameworks. Finally, for what they dub as newly emerging clusters based on external investment, ideal policies include anticipating the requirements of the cluster for skilled labor and infrastructure and encouraging innovation for local enterprises to qualify as suppliers.

Several case studies have been used to further argue for the tailor-fitting of policies to the type of cluster. So-called “dynamic” type of clusters, which already enjoy extensive export networks and intraindustry specialization, are said to benefit from a policy focused on technical upgrading, export training, and investment in regional infrastructure as demonstrated by the case of the Jepara wooden furniture cluster in Central Java, Indonesia.¹²⁶ The government’s development package, which also included the creation of an industrial estate, a shared showroom, and support for trade fairs, has led to the area becoming “a

123 Van Dijk, Meine Pieter and Árni Sverrisson. (2003). Enterprise clusters in developing countries: mechanisms of transition and stagnation. 15 *Entrepreneurship & Regional Development*: 201.

124 Knorringa, Peter & Jörg Meyer-Stamer. (1998). New dimensions in local enterprise cooperation and development: from clusters to industrial districts. *New Approaches to Science and Technology Cooperation and Capacity Building*: 16.

125 Knorringa et al., 17.

126 Tambunan, Tulus. (2005). Promoting small and medium enterprises with a clustering approach: A policy experience from Indonesia. 43-2 *Journal of Small Business Management*: 148.

leading exporter of wooden, rattan, and metal furniture.”¹²⁷ Tambunan warns, however, that much of the failure in Indonesian experience had to do with neglecting the development of access to growing markets and policy makers would do well to avoid this pitfall.

Altenburg and Meyer-Stamer, for their part, identified different types of clusters across Latin America and the corresponding policy for their development. The Chilean initiative of *Proyectos de Fomento*, for instance, was geared toward so-called “survival clusters” that have low innovation and specialization.¹²⁸ Through a three-year contract between a group of SMEs and a support agency, the clusters received funding for “market surveys, feasibility studies or participation in trade missions and fairs.”¹²⁹ This was said to have been the “most successful example of how to promote associations of SMEs in Latin America.”

More advanced clusters, like the Itajai valley textiles and garment industry in Brazil, were given support focused on improving cooperation among the enterprises to boost innovation adaptation. The successful initiative in this case was a benchmarking exercise in 1997, which brought in experts from a Switzerland-based organization and helped firms become “more open-minded, also because a leading local industrialist assumed the role of an agent of change.”¹³⁰

Clusters of the transnational type, meanwhile, are said to respond well to programs like subcontracting exchange schemes which encourages technology spillover from the foreign buyer and into the local enterprises as long as the scheme uses an “integrated approach [that involves] combining matchmaking with specific support for potential suppliers.”¹³¹

Sandee and Rietveld, commenting on upgrading SME clusters, similarly noted that support focused on access to information and joint action likewise helped the tile cluster in Karanggeneng, Indonesia, to adopt new technology and thus innovate.¹³²

In a similar vein, Bergman and Fesser recommend policy sensitivity to the characteristics of a cluster as their experience in North Carolina, United States showed that firms’ tendency to co-locate or to adopt technology can depend on their type of sector or the size of the establishments in a cluster. Motor vehicle supplier chains, for

127 Ibid.

128 Altenburg, Tilman & Jörg Meyer-Stamer. (199). How to promote clusters: policy experiences from Latin America. 27-9 *World development*: 1696.

129 Ibid.

130 Altenburg et al., 1702.

131 Ibid.

132 Sandee, Henry and Piet Rietveld. (2001). Upgrading Traditional Technologies in Small-Scale Industry Clusters: Collaboration and Innovation Adoption in Indonesia. 37-4 *Journal of Development Studies*: 156.

instance, were observed to arrange themselves in corridors, while those dependent on natural resources were more highly dispersed.¹³³ As such, the authors warn that these “co-location tendencies should give pause to those advocating cluster-enhancing policies based on routine assumptions that all cluster firms now, or are willing to, locate within very short distances.”¹³⁴

It is clear from the above review of relevant case studies that formulating an industrial clustering strategy requires an understanding of the level of development of SMEs and their specific needs and resources, among others. This will be facilitated at the outset by addressing the present incoherence in SME development policies and implementation and poor coordination among implementing agencies.

It is also clear that simply adopting an OTOP program cannot sufficiently address the challenges in building industrial clusters or maximize the opportunities that global markets present to Philippine SMEs.

E. Promote Linkages Between and Among SMEs and LEs in Various APEC Economies or Other Regional Groupings

The Philippines and other APEC economies should maximize programs and initiatives of APEC related to its objective¹³⁵ of promoting economic and technical cooperation for development among its economies.

F. Foster Benchmarking and Networking Among SMEs Through Publications and Fora

APEC can also be the best avenue to promote benchmarking information of SMEs in all countries. Best practices can be shared and disseminated more easily by APEC. It can hold regularly fora and symposia on benchmarking and information-sharing activities, which will also be a great avenue for networking. Publication of timely and relevant information can also be done by APEC and this will surely and equally benefit developed and developing economies.

133 Bergman, Edward M. and Edward J. Feser. (1999). Industry clusters: A methodology and framework for regional development policy in the United States. Boosting innovation: the cluster approach: 254.

134 Ibid.

135 APEC's Bogor Goals articulates the primary objectives of APEC: (a) trade and investment liberalization, (b) trade and investment facilitation, and (c) economic and technical cooperation for development.

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