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## **ASEAN Community: Economic Integration and Development of SMEs**

*By Ong Keng Yong & Phidel Gonzales Vineles*

### **Synopsis**

*The ASEAN Community is in business notwithstanding various challenges. The huge potential of ASEAN Small and Medium Enterprises must be tapped to strengthen the backbone of the regional economy.*

### **Commentary**

AS ASEAN celebrated its 49th anniversary on 8 August 2016, regional public opinion is sceptical that the ASEAN Community exists. The fact is each ASEAN Member State does not count for much in the global economy even though Indonesia, as the biggest economy in Southeast Asia, is seen as quite significant with a GDP of nearly US\$900 billion. But that is only the size of the economy of Tokyo, the capital area of Japan. The combined GDP of ASEAN Member States is about US\$2.6 trillion. This makes ASEAN the seventh largest economy in the world. In ten years' time, ASEAN can overtake the United Kingdom and France to be No.5 – after the US, China, Japan and Germany!

### **ASEAN Community: New Operating Environment**

ASEAN is very diverse – 10 different cultures, economic systems, history and political order. The ego of each nation in the grouping is typically self-centred. That creates troubles for the organisation from time to time. Yet, looking at the global picture, forming the ASEAN Community is a strategic imperative and economic necessity.

Collectively, the Southeast Asian countries as ASEAN will be competitive vis-a-vis other regions of the world and an attractive destination for investors. ASEAN needs

foreign direct investment and jobs for its peoples. ASEAN will do well if the member states work together and navigate through the interests of powerful neighbours and the bewildering technological developments affecting the marketplace and society.

The ASEAN Community is now the operating environment for all of us. The ASEAN Community has three pillars – political/security, economic and socio-cultural. The ASEAN Economic Community or the AEC has achieved positive results even though there are persistent complaints that ASEAN businesses are still not fully aware of the benefits accruing from the AEC. Tariff reduction and removal of obstacles to facilitate trade and open markets are ongoing. ASEAN is amalgamating its five Free Trade Agreements (FTAs) with China, Korea, Japan, Australia/New Zealand and India into the Regional Comprehensive Economic Partnership (RCEP). Infrastructural development and connectivity are being improved. Overall, growth prospects for the AEC are good: more than 5% annually for the next five years.

### **ASEAN SMEs: Significant Growth Engine**

To be sure, ASEAN could do better and it has prioritised the development of small and medium enterprises (SMEs) to achieve equitable, inclusive and sustainable growth, as they represent more than 95% of all enterprises in the region. This could also contribute to poverty reduction as well as improve the status of women in the region as almost half of the enterprises are women-owned.

ASEAN SMEs are the backbone of the ASEAN economies. According to the ASEAN Secretariat, they employ between 52% and 97% of all workers. In addition, their contribution to each ASEAN Member State's GDP varies between 30% and 53%. However, their share of total exports remains small, between 10% and 30%. This means much remain to be done to strengthen the role of SMEs to help ASEAN economic integration.

The ASEAN Strategic Action Plan for SME Development laid out five key strategies: (1) promote productivity, technology and innovation; (2) increase access to finance; (3) enhance market access and "internationalisation"; (4) enhance policy and regulatory environment; and (5) promote entrepreneurship and human capital development.

### **SMEs Not Equipped for AEC and RCEP?**

Several analysts claimed that most SMEs in the region are not fully equipped to deal with new business realities of the AEC and the RCEP. The AEC is an integrated market and production base of over 620 million people, which could expand to more than three billion through the RCEP. Both the AEC and the RCEP could bring many opportunities for the SMEs, realise economies of scale for them and increase their participation in the global value chains.

However, it is projected that SMEs will face intense competition from the entry of multinational corporations (MNCs) and cheap imports. Hence, ASEAN Member States should fine-tune their concrete action lines in relation to the specific needs and circumstances of their SMEs.

Productivity and technology improvements are key drivers of SMEs to integrate with the production networks of MNCs. These drivers could be further enhanced if SMEs are allied with other SMEs or with large enterprises. However, there are some challenges to boost productivity of ASEAN SMEs.

According to various studies, average labour productivity (GDP per person employed) in ASEAN was equivalent to only 31% of US labour productivity in 2015. There are notable variations on labour productivity among ASEAN Member States: Singapore's average labour productivity equivalent to US' labour productivity is 112%, Thailand (25%), Myanmar (8%), and Cambodia (5%).

There should be more training within ASEAN SMEs to help boost their labour productivity to levels needed to become qualified suppliers in global value chains. SMEs should also invest in specialised technical training for their workers.

### **Overcoming Impediments to SME Development**

According to the Economic Research Institute for ASEAN and East Asia (ERIA), the lack of strategic approach to innovation policy for SMEs is one of the impediments of SME development in ASEAN. It is therefore necessary to find ways to promote technology and technology transfer for developing SMEs' innovation capabilities. Protection and promotion of intellectual property rights, development of broadband infrastructure and industrial parks, and sufficient financial incentives in research and technology development are some policy measures which have to be instituted to boost the SMEs.

Access to finance is a key concern for ASEAN SMEs. According to ERIA, there is a big gap in the access to finance of the less developed ASEAN Member States when compared with Singapore, Malaysia, Thailand, Indonesia, and the Philippines. There are also cumbersome requirements. According to the World Bank, an average of 47 days is required for 13 procedures to start a business in Indonesia, while it requires 73 days for six procedures in Lao PDR. It would only take three days to complete three procedures in Singapore and online electronic applications are made to a single authority. The business registration process should be simplified.

Promoting human resource development and entrepreneurship is essential for SMEs to succeed. Entrepreneurship learning programmes help equip SMEs with improved management and business methods. Presently, the ASEAN Common Curriculum in Entrepreneurship, which is one of the initiatives of ASEAN Strategic Action Plan for SME Development, aims to establish a common curriculum for entrepreneurship in the region with the use of an entrepreneurship educational programme that is currently implemented in ASEAN universities.

In conclusion, it is essential to implement an effective SME development policy that will propel regional cooperation among ASEAN Member States. This will assist SMEs to expand internationally and integrate them into global supply chains.

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