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**Dr. Mohamad Saad Abo Karesh**

Assistant Professor at Faculty,  
Department of Economics and  
Political Science, Bani Walid,  
Libya

## The role of small and medium enterprises in supporting economic development: Evidence from Malaysia

**Dr. Mohamad Saad Abo Karesh**

### Abstract

This study explored role of small and medium enterprises in supporting Malaysian economic development. The study reached a set of results, the most important of which is that small and medium enterprises contribute up to 35.9% to the gross domestic product, the added value of small and medium enterprises is 36.3%, and the employment rate is 65.5% of the total workforce in Malaysia. The most prominent challenges facing small and medium enterprises in Malaysia are the limited capacity to manage technology and acquired knowledge.

**Keywords:** Gross domestic product, added value, and employment rate

### Introductions

The interest in small and medium enterprises in Malaysia began in the early seventies with the implementation of the New Economic Policy in 1971, which aimed to improve the standard of living and restructure economic imbalances. The commitment of the Malaysian governments to the development of small and medium enterprises has been strengthened through the implementation of the Industrial Master Plan in Malaysia, in particular the Second Industrial Master Plan from 2000 to 2005, which was followed by the Third Environmental Management Plan that extends from 2006 to 2020. And which coincides with the comprehensive vision that aims to: Malaysia is a developed country by the year 2020 and as a result of the important role of small and medium enterprises, the Malaysian state is working on designing and implementing plans for developing small and medium enterprises to help them face new challenges, especially in the field of global competition. In Malaysia, Small and medium-sized enterprises (SME) represent about 99% of all businesses and contribute 35.9% to the country's Gross domestic product (GDP). Moreover, SMEs employ 65% of the total workforce and generate 30% of the total exports.

Considering that the Malaysian experience in the field of small and medium enterprises is one of the successful experiences, which greatly contributed to achieving a remarkable development of the Malaysian economy and a diversification of sources of income. Therefore, this study deals with research and analysis of small and medium enterprises in Malaysia and their role in achieving economic development by focusing on the contribution of small enterprises. In addition to focusing on government policy on enhancing the competitiveness of small and medium enterprises and methods of government financing for small and medium enterprises, and shedding light on the challenges they face.

### Problem Statement

Although Malaysia has one of the best economic records in Asia and was the third largest economy in Asia and the 29<sup>th</sup> in the world, and despite the fact that small and medium enterprises contribute significantly and significantly to increasing the national income in Malaysia, increasing state revenues, improving the standard of living for individuals and diversifying the sources of income for the state. However, there are many circumstances that require investigation to reach economic stability and achieve comprehensive development in Malaysia, and thus the problem can be formulated in the following question: To what extent do small and medium enterprises contribute to achieving economic development in Malaysia?

**Corresponding Author:**

**Dr. Mohamad Saad Abo Karesh**  
Assistant Professor at Faculty,  
Department of Economics and  
Political Science, Bani Walid,  
Libya

### Significance of the Studying

The significance of the study is evidenced by the fact that it is related to a topic that was and still occupies a prominent position in the field of scientific research on the one hand, and many organizations, institutions and countries are interested in it, and it is small and medium enterprises that increase their importance and increase their role day after day because of their money role in raising the rates of economic growth, reducing unemployment and improving the standard of living. Moreover, the importance of research lies in shedding light on the experience of the State of Malaysia in this field, through which it has achieved growth in all economic variables and tangible development in all fields.

### Research Questions

1. What is the extent of the contribution of small and medium enterprises to the Malaysian economy?
2. How successful are the Malaysian state policies in developing small and medium enterprises?

### Methodology

The main objective of the study is to review the Malaysian experience in the field of small and medium enterprises and to identify the extent of their success and the policies that were followed to develop them. Therefore, the study will depend on the descriptive and analytical approach by presenting, describing and analyzing data.

### Previous Studies

Noraini, (2015) <sup>[7]</sup> explored the determinants of the performance of SMEs in the services sectors in Malaysia. Based on the data collected from 400 SMEs in the Malaysian services sector, the results showed that there are important positive relationships between human resources management and the orientation towards. The results also indicate that human resources management and market orientation are the most important influencing factors among the determinants.

Arunagiri, *et al.* (2015) <sup>[2]</sup> focused on the various factors that affect small and medium enterprises such as workers' wages, unemployment rates, net exports and the rate of inflation. The study found that labor wages and net exports are the main factors that contribute significantly to the performance of small and medium enterprises. The study recommends the necessity to focus on these factors to enable Malaysian small and medium enterprises to improve their performance and contribute to national production.

Siti Sarah, (2009) <sup>[8]</sup> focused on the most important challenges facing small and medium enterprises in Malaysia, which play an important role in achieving economic growth. The study focused on the challenges facing human resources in particular, which have a role in developing and supporting small and medium enterprises.

In a similar study, Hala *et al.* (2014) <sup>[5]</sup> explored small and medium enterprises in Egypt and the main results showed that the geographical distribution of small and medium enterprises is almost half concentrated in the three governorates of the East, Cairo and the West. They operate mainly in two economic activities: manufacturing and trade. Also, small and medium enterprises do not benefit from financial services, but only 50 percent of them deal with banks and benefit from improving access to finance.

Also, Sherif (2008) <sup>[4]</sup> explored small and medium enterprises in Algeria by focusing on their reality, strategies for their development and the problems they face. The study emphasized the need to pay more attention to small and medium enterprises and the need to develop the economic media by establishing an economic and statistical database and providing a suitable investment climate to ensure their success. Hussein, (2005) <sup>[3]</sup> also dealt with small and medium enterprises and their role in employment and job creation in Arab countries through Recognizing its importance for the Arab countries, as well as showing the importance of the challenges facing the development of these projects.

### Defining Small and Medium Enterprises in Malaysia

The term small and medium enterprises is a widespread term, and opinions are gathered on the growing importance of its role in the national economy, whether in developed or developing countries alike, especially in light of the increasing need to generate employment opportunities. Despite this, there is no specific definition of small and medium enterprises due to the difference in the size of the economy. Country to country in addition to the different countries in terms of economic resources and population size, and projects are classified in Malaysia to small and medium scale, depending on two basic criteria: the number of employees and the value of sales as follows:

First, depending on the criterion of the number of employees

- a) The industry sector

The project is considered small if the number of workers ranges between 5 to 50 workers

- The project is considered average if the number of workers ranges between 51 to 150 workers

- b) the services and agriculture sector

The project is small if the number of workers ranges between 5 to 19 workers

The project is medium if the number of workers ranges from 20 to 50 workers

Second, depending on the sales value criterion

- a) The industry sector

The project is considered small if the sales value is from 250,000 RM to 10 million RM (in Malaysian currency, ringgit)

The project is considered average if the sales value is from 10 million RM to 25 million RM

- b) The services and agriculture sector

A project is small if the sales value is from 200,000 to 1 million RM

- The project is medium if the sales value is from 1 million RM to 5 million RM

### The Development of the Number of Small and Medium Enterprises in Malaysia

Small and medium enterprises have received great attention from the Malaysian state, believing in its role in achieving the required growth rates and its ability to absorb employment, provide job opportunities and reduce the burden on the state. Therefore, many policies, programs and plans have been developed that will support and develop

these projects. The government has embarked on promoting entrepreneurship to enhance the role of small and medium enterprises as an important goal to achieve balanced economic development and higher standards of living for all segments of society.

The government has put in place a solid regulatory framework, necessary physical infrastructure, as well as incentives to encourage the participation of small and medium enterprises in these areas. For its part, the government continues to play a facilitating role in creating an enabling business environment to ensure the development of small and medium-sized enterprises to their fullest potential as a major driver of economic growth. These policies were reflected in the increase in the number of small and medium enterprises, which increased from 518,996 companies in 2005 to 771,286 companies in 2015.

**Table 1:** Evolution of the number of small and medium enterprises in Malaysia

Year	2005	2010	2015
Number of enterprises	518,996	645,136	771,286

The table was prepared by the researcher based on statistical reports for different years.

**The Contribution of Small and Medium Enterprises to the Malaysian Economy**

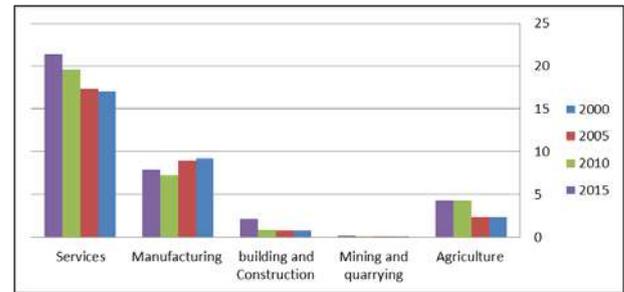
The Malaysian government has prioritized the development of SMEs on the national agenda by developing a competitive, productive and flexible SME sector in order to achieve balanced economic development with higher standards of living. This contrasts completely with the situation in the past when Malaysian economic growth was mainly driven by the export and investment of multinational companies.

With regard to the contribution of small and medium enterprises to the gross domestic product in the period 2000-2015, where the services sector contributed by 17.1% in 2000, then this percentage increased to 21.4%, followed by the sectors of industry, construction and agriculture. It is noticeable that the contribution of small and medium enterprises in the mining sector decreased, which did not exceed 0.2% 2015. Despite the global financial crisis in 2009, the average annual growth rate for small and medium enterprises in the period 2006-2009 was 5.7%, higher than the average macroeconomic growth of 3.8%. It should be noted that despite the economic slowdown, SMEs continued to perform better than the overall economy (SMEs Annual Report 2009/2010). Through Table (2) and Chart (1), the extent of the contribution of small and medium enterprises to the gross domestic product, as their contribution increased from 29.55% to 35.9%, confirms the increasing role and contribution to the activity especially economic and it is more durable than large companies during an economic downturn. They are growth stabilizers and are able to adapt to changes in market conditions efficiently.

**Table 2:** Percentage of SMEs' contribution to the GDP.

years	2000	2005	2010	2015
Agriculture	2.4	2.4	4.3	4.3
Mining and quarrying	0.05	0.04	0.05	0.2
building and Construction	0.8	0.8	0.9	2.1
Manufacturing	9.2	9.0	7.2	17.9
Services	17.1	17.3	19.6	21.4
total	29.55	29.54	32.05	35.9

The table was prepared by the researcher based on a group of reports for different years



**Source:** prepared by the researcher based on the data contained in the previous table

**Fig 1:** Contribution of Small and Medium Enterprises to the Gross Domestic Product by Sector

**Added Value and Commission Rate in Small and Medium Enterprises**

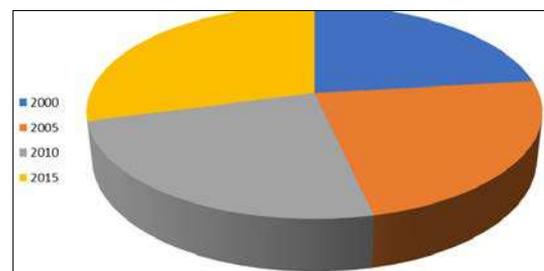
The growth of the added value of small and medium-sized companies achieved momentum at its peak, reaching 36.3% in 2016 compared to 28.8 in the year 2000, and this enhances the role of small and medium enterprises in providing the needs of goods and services and increasing the contribution of economic sectors to economic activity.

**Table 3:** Shows the added value and the percentage of employment in small and medium enterprises

year	2000	2005	2010	2015
Value added	30.2	28.8	29	30
Employment to total workforce ratio	57.3	53.2	56.4	65.5

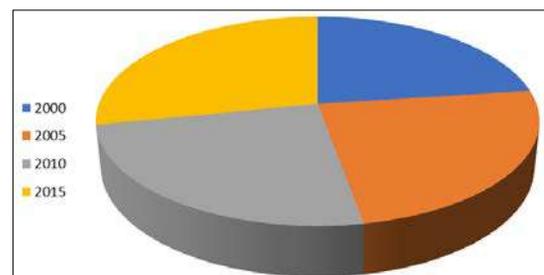
The table was prepared by the researcher based on a group of reports for different years

In addition, small and medium enterprises absorb a large number of workers in Malaysia, as they absorb 65.5% of the total workforce in 2015, while they absorbed 53.2% of the workforce in 2000, and this in turn enhances the status of small and medium enterprises and their role in providing opportunities. Work and reduce unemployment.



**Source:** Prepared by the researcher based on the data contained in the previous table

**Fig 2:** The added value of small and medium enterprises



**Source:** prepared by the researcher based on the data contained in the previous table

**Fig 3:** The ratio of employment in small and medium enterprises to the total workforce

### **Government Policy on Enhancing the Competitiveness of Small and Medium Enterprises**

The development of a competitive, small and growing enterprise sector is a major component of the Malaysian government's economic growth strategy. Whereas the small and medium enterprises sector in 2010 constituted 99.2% of the total commercial establishments and employed more than 57.3% of the total employment in the country. The government has embarked on promoting entrepreneurship in small and medium enterprises, as it is an important goal to achieve balanced economic development and higher living standards in all segments of society. In 2010, the SME sector contributed 32% of the real GDP and 19% of the total value of Malaysian exports (Nik & Shahrul, 2011) <sup>[6]</sup>.

In 2006, the government implemented a total of 213 major programs, with total expenditures amounting to RM7.8 billion. The main focus of these programs was on strengthening the capabilities of small and medium enterprises, particularly in the areas of entrepreneurship development, marketing and promotion, product development and technology promotion. More than 287,000 enterprises have benefited from the implementation of these small and medium programs.

In 2007, a total of 189 programs were launched with a financial commitment of 3.7 billion rand (Small and Medium Enterprise (SME) Annual Report 2007). These programs focused on capacity building, human capital development, as well as marketing and promotion. Specific programs have also been developed to strengthen links between small and medium enterprises, large domestic companies, as well as multinational companies. These linkages also provide a valuable tool for small and medium-sized enterprises to develop strong technical, competitive and innovative capabilities as well as managerial and business skills.

The government has put in place a solid regulatory framework, necessary physical infrastructure, as well as incentives to encourage the participation of small and medium-sized enterprises in these areas, and to play a facilitating role in creating a favorable business environment to ensure the development of small and medium-sized enterprises to their fullest potential as a major driver of economic growth.

### **Government Funding for Small and Medium Enterprises**

Access to finance is an important aspect of the business operations of SMEs. In addition, with the ever-changing needs of SMEs, various initiatives have been taken to strengthen the existing financing providers and expand financing avenues for SMEs. 2007 saw a wide range of financing available to SMEs in various stages of their life cycle such as start-ups, business expansion and rehabilitation (Small and Medium Enterprise (SME) Annual Report 2007).

### **The Main Players Supporting the SME Sector in Malaysia**

Given the importance of these projects considering that they have a major role in the development of the Malaysian economy, the Malaysian state has given them much attention, which is reflected in the multiplicity of institutions supporting small and medium enterprises as follows:

### **The National Council for Small and Medium Enterprises Development**

The establishment of the National Small and Medium Enterprise Development Board in 2004 as the highest policy-making body marked another chapter in the development of SMEs in Malaysia. The council provides policy directions for achieving coherent and comprehensive development of SMEs. It is chaired by the Prime Minister of Malaysia, while the Central Bank of Malaysia takes the role of the secretariat to the Board, but now it is the Small and Medium Enterprises Institution of Malaysia. Fifteen ministries and more than 60 government agencies work together to achieve a common goal of developing small and medium-sized enterprises that are competitive and competitive by world standards.

### **Small and Medium Industries Development Company**

The Small and Medium Industries Development Corporation was established on 2 May 1996 as a specialized agency to encourage the development of small and medium enterprises through the provision of infrastructure facilities, financial assistance, advisory services, market access and other support programs. The ultimate goal was to develop adaptive SMEs to be able to compete in the global market. In 2007, the National Coordination Committee decided to appoint one dedicated agency to assume the role of the central coordination agency by formulating general policies and strategies for SMEs and coordinating programs across all relevant ministries and agencies.

### **Central Bank of Malaysia**

The Central Bank of Malaysia was established on 26 January 1959 under the Central Bank of Malaysia Act 1958 (Amendment 1994). The bank is a legal entity wholly owned by the Government of Malaysia. The report is submitted to the Minister of Finance.

### **Credit Guarantee Company**

Helping small and medium enterprises, especially those that do not have guarantees or a proven track record, with insufficient guarantees to obtain credit facilities from financial institutions by providing guarantee coverage on these facilities; A credit guarantee company was incorporated on July 5, 1972.

### **Small and Medium Business Credit Bureau**

The SME Credit Rating Bureau was established on 3 June 2008 by the Credit Guarantee Corporation to be the leading provider of credit reports for SMEs in Malaysia that helps in the rapid assessment of any SME creditworthiness. By gathering key information available for the company's performance.

### **Agricultural Bank**

The Agricultural Bank was formed under Berhadan Malaysia Bank Berhad on April 1, 2008; whereas, Bertanian Bank was originally incorporated in the year 1969.

### **Challenges of Small and Medium Enterprises in Malaysia**

Small and medium enterprises in Malaysia still face many local and global challenges in order to compete internationally. Among the main constraints that SMEs face are managerial capacity and a skilled workforce; Access to

finance and markets; Inability to exploit economies of scale and lack of bargaining power; Low technology, limited access to international markets. Procedures and regulations also disproportionately affect small and medium firms compared to large firms. Saleh and Ndubisi (2006) <sup>[9]</sup>. Finance is one of the critical success factors that have been identified to fund the establishment and future expansion of the corporation. According to a performance monitoring survey by CMC Malaysia in 2010 and 2011, the results indicated that the increase in the cost of raw materials Inputs are the main constraints in doing business. In addition, another problem that SMEs often face is access to research and development. In addition to these difficulties, SMEs also find it difficult to enter the market. Malaysia's other challenges can be summarized as follows:

1. Intensification of global competition
2. Competition from other producers
3. Limited capacity to face the challenges of market liberalization and globalization
4. Limited ability to manage technology and acquire knowledge
5. Low productivity and production quality
6. Lack of skills in the new business environment
7. Limited access to finance and capital, in the early stages of the project
8. The high cost of infrastructure
9. A general lack of knowledge and information

### Results

1. Small and medium enterprises contribute 35.9% to the gross domestic product of Malaysia in 2016
2. The added value of small and medium enterprises reached 36.3%, and the employment rate reached 65.5% of the total workforce in Malaysia
3. Small and medium enterprises in the services sector contribute more than enterprises operating in other sectors, either to the gross domestic product or to the absorption of labor.
4. Small projects received wide attention from the Malaysian authorities, which contributed to their development and contribution to enhancing the development process and working to improve the standard of living of individuals.
5. One of the main challenges facing small and medium enterprises in Malaysia is the limited ability to manage technology and acquire knowledge.

### Recommendations

1. Providing support and training for owners of small and medium enterprises in all stages of the production process, so that there is no interruption in the production and marketing process, and thus in the financing process.
2. Facilitating obtaining financial support for small and medium enterprises, especially successful ones, to ensure their continuity and expansion, and to assist stalled projects with funds and consultations.
3. Supporting small and medium enterprises by working to open markets for them at home and abroad with the need to focus on quality to ensure their ability to compete.
4. Paying attention to training the workforce in the field of small and medium enterprises to gain knowledge and

manage modern technology that contribute to developing small and medium enterprises.

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