International Trade Centre

TRADE IMPACT FOR GOOD

Promoting SME competitiveness in the Philippines

Compete, connect and change to build resilience to crises

In collaboration with

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Street address:	ITC 54-56, rue de Montbrillant 1202 Geneva, Switzerland
Postal address:	ITC Palais des Nations 1211 Geneva 10, Switzerland
Telephone:	+41-22 730 0111
Fax:	+41-22 733 4439
E-mail:	itcreg@intracen.org
Internet:	http://www.intracen.org

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About the paper

Increasing the competitiveness of small firms in the Philippines is vital to build resilience to shocks while promoting sustainable and inclusive growth.

Companies that were more competitive before the COVID-19 crisis were less affected by it, according to ITC's SME Competitiveness Survey. Firms with a greater capacity to change – because of their skills, innovation and financial management – were more likely to adopt resilient or agile responses. Finally, those with better connections to their business ecosystem were better able to access the information and support they needed to survive the crisis.

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For more information, contact: Valentina Rollo, rollo@intracen.org

For more information on SME Competitiveness Survey, see http://www.intracen.org/SMEintelligence/

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Foreword

The COVID-19 crisis has taken a huge toll on small companies in the Philippines. The economy is expected to shrink by 2% in 2020 after expanding 5.9% in 2019 and with unemployment projected at 6.8% in 2020, the Philippine government has prepared an emergency response plan focusing on higher health spending, monetary stimulus, cash transfers and support to affected firms.

Small and medium-sized enterprises (SMEs) employ 60% of the Filipino workforce. These firms are instrumental to achieving *AmBisyon Natin 2040*, the national vision for a strongly rooted, comfortable, and secure life for all Filipinos.

Helping these companies become more competitive would unleash their potential to flourish in the post-COVID-19 era. The 'new normal' in trade will stress resilience to shocks, embrace digital opportunities, provide inclusive employment opportunities, and prioritize environmental sustainability.

Transformative policymaking can help small firms take advantage of the trading opportunities on the horizon. However, up to date and accurate data and analysis will be critical in highlighting the constraints that these SMEs face, as well as their strengths and opportunities.

To this end, the Department of Trade and Industry of the Philippines (DTI), through the Bureau of Small and Medium Enterprise Development (BSMED), partnered with the International Trade Centre (ITC) to assess the competitiveness of small Filipino firms and the impact COVID-19 had on their ability to compete and trade globally. More than 450 companies were interviewed for the SME Competitiveness Survey (SMECS) and the ITC COVID-19 Business Impact Survey in the Philippines.

This report presents what the surveys revealed about the competitive strengths and weaknesses of Filipino SMEs and how that affected how they coped with the COVID-19 crisis. The findings will help in the design of policies and programmes that create a competitive and resilient SME sector that can withstand future shocks, whatever their nature or origin.

ITC and DTI share a common vision to build the competitiveness of small firms so they can access more local, regional and global markets and better adapt to shocks. Trade can fuel growth, generate income and reduce poverty, especially if appropriate domestic policies are in place. We see this report as an important step to make this vision a reality.

Pamela Coke-Hamilton
Executive Director
International Trade Centre

Ramon M. Lopez
Secretary
Department of Trade and Industry

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Acronyms

Unless otherwise specified, all references to dollars ($) are to United States dollars and all references to tons are to metric tons. Percentages in some figures and tables may not add up to 100% due to rounding.

APEC	Asia-Pacific Economic Cooperation
ASEAN	Association of Southeast Asian Nations
BSMED	Bureau of Small and Medium Enterprise Development
BSO	Business support organization
DTI	Department of Trade and Industry
ECQ	Enhanced community quarantine
ITC	International Trade Centre
MSMEs	Micro, small and medium enterprises
R&D	Research and development
SMEs	Small and medium-sized enterprises
SMECS	SME Competitiveness Survey

Executive summary

Small and medium-sized enterprises (SMEs) are the economic lifeblood of the Philippines. They account for more than 99% of registered businesses in the country and provide 60% of jobs.

The COVID-19 crisis has made it more difficult for these firms to participate in global value chains. Increasing the competitiveness of small companies can spur resilience to the pandemic and future shocks while promoting inclusive and sustainable growth.

Empirical evidence on the strengths and weaknesses of SMEs can pinpoint opportunities to improve their competitiveness and resilience. To set this process in motion, the International Trade Centre (ITC) partnered with the Bureau of Small and Medium Enterprise Development (BSMED), part of the Department of Trade and Industry (DTI) of the Philippines, to assess the competitiveness and resilience of small firms across the country.

The SME Competitiveness Survey was administered to 514 businesses in Metro Manila, Central Luzon, Calabarzon and Cebu City regions in late 2019. Responses from 454 of these firms to the ITC COVID-19 Business Impact Survey in early 2020 complemented the competitiveness survey.

This report analyses data from both surveys, identifying challenges and strengths in firm capabilities and the business ecosystem, and how they affect resilience. Although the focus is on small enterprises, large companies are included in the analysis for the sake of comparison.

Analysing different aspects of competitiveness yields insights into economic realities. A specific focus on how small Filipino companies compete in certain sectors and regions – and when they are led by women or youth – shows the detailed pattern of competitiveness across enterprises.

This report, along with complementary events and collaborations, disseminates the results in the hopes of triggering an evidence-based dialogue on policies to promote SME competitiveness and resilience in the Philippines.

COVID-19 has strongly affected most Filipino firms

Findings from the ITC COVID-19 Business Impact Survey suggest that almost all (99%) interviewed firms were affected, with more than two-thirds saying they had been strongly affected. While manufacturers were more likely to say they had been strongly affected by the pandemic, the effects on all interviewed businesses were pervasive, everything from lower sales (88% of respondents) and difficulty accessing inputs (86%) to reduced logistics services (46%) and clients not paying bills (33%).

In the face of this shock, resilient companies were better able to get through the pandemic. A third of interviewed Filipino companies proved resilient, adopting strategies such as shifting the sales mix towards online channels or finding new suppliers. Enterprises that were more competitive before the crisis hit, and which participated in international trade, tended to be more resilient.

Filipino companies that participated in the COVID-19 survey said that tax waivers, temporary tax breaks and cash transfers would be the most helpful government measures to help them deal with the crisis.

Transparency and information are vital for firms to benefit from government assistance programmes. It is therefore worrisome that 58% of survey respondents in the Philippines found it difficult to access information and benefits from government COVID-19-related assistance packages.

The harsh impact of the pandemic led 9% of interviewed companies to say they expected to shut down permanently as a result. SMEs were twice as likely as large firms to predict their own closure within three months.

Management skills affect how firms compete

Empirical evidence from the competitiveness survey indicates that most Filipino companies can produce goods that customers want at a reasonable cost. Half said they delivered all of their output on time, and 44% described their inventory management techniques as highly efficient.

However, poor cash flow is hampering the ability of many firms to compete on lucrative terms. Half said they lacked good cash flow management. Many buyers do not pick up and pay for their orders on time, hurting the liquidity of the seller and forcing it to compete on shaky, non-remunerative grounds to get cash in the short term – for example, by

offering low prices. Companies with better cash flow tended to compete by selling more lucrative higher-quality products or bulk orders.

More competitive firms were less affected by COVID-19

Companies that were better able to compete before the pandemic were less likely to be strongly affected by it. Just 57% of firms with full capacity utilization – a measure of the extent to which a company is using its production potential – said the pandemic had a strong impact on their businesses, compared to 68% of all companies that participated in the survey.

Firms that described their inventory management as 'highly efficient' or said they had a 'very good' ability to manage their cash flow were also less likely to report a strong impact. Better management skills and supply-side capacity help protect companies from shocks.

Small companies excel in skills and innovation

The Philippines performs quite strongly in measures of competitiveness for the knowledge economy. Four out of five respondents to the SME Competitiveness Survey were satisfied with the workforce skills in their enterprise, and two out of three said they frequently developed new goods or services.

Entrepreneurial characteristics affect firm capacities. Women-led companies tend to dedicate fewer resources to innovation, so they did not have many new products and processes. Youth-led, micro and small enterprises also perform relatively poorly on innovation.

Innovative firms were more resilient to the COVID-19 crisis

Companies that can use skills, financing and innovation to change are better able to shift with market trends. This adaptive capacity is essential to building resilience to crises, because firms that already have the tools and


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habit of changing have the adaptive capacity to ride out the storm.

Participation in the knowledge economy helped many Filipino firms cope with COVID-19. Companies that invested more resources in research and development before the pandemic were more resilient or agile, and less likely to adopt a retreating response to the crisis. This suggests they were familiar with and able to take strategic initiatives for the long-term welfare of the enterprise.

Stronger connections foster access to information

Filipino firms have relatively weak connections to the buyers, suppliers and business support organizations in their business ecosystem. Only one in four surveyed companies had engaged with a business support organization, and just three-fifths connected to their buyers through production specifications, international trade, ownership or other coordinated value chain linkages. Half of interviewed firms advertise, and when they do, it is mainly through Facebook or the internet.

Companies with connections to their buyers seem to be more competitive. They deliver a higher proportion of output on time, advertise and innovate more, and are better able to prepare a business plan. Facilitating buyer connections for the 36% of unconnected firms would help spur advertising and competitiveness.

Better engagement with business support organizations is also associated with greater competitiveness, as it helps firms access market information on new suppliers and exchange information with each other. As already noted, it is especially crucial to access the information and help needed to survive a crisis.

Connections helped firms get information about COVID-19

The experience with COVID-19 shows that access to information was crucial in the days and weeks that followed the initial shock. Companies with strong connections to their buyers, suppliers and business support organizations had a ready network available for support when the pandemic hit.

Evidence from the SME competitiveness and COVID-19 surveys indicates that firms with better connections to their business ecosystem were better able to access the information and support they needed to survive the crisis. Being engaged with a business support organization, such as a chamber of commerce, made it easier to find information and obtain benefits. This is important, because fewer companies with good access expected to go bankrupt.

Policies to improve competitiveness

Several policy recommendations emerge from the survey findings, the most important being the need to strengthen the connections between SMEs and their business ecosystem. There is an opportunity to enhance the outreach from business support organizations to additional small businesses.

Poor cash flow prevents many small Filipino firms from effectively engaging in local and international markets. A careful look at government public procurement plans, and specifically their provisions for timely payment and reservations[1] to SMEs, could help address this issue.

Although the Philippines generally excels when it comes to the dynamism of its businesses, the next step for policymakers is to extend programmes for skills, research and innovation to all companies. Customizing skills training sessions to ensure that enterprises headed by youth and women can access suitably skilled workers would make it easier for them to innovate and change.

Looking towards the long term, the government needs to ease the transition of small firms to the 'new normal' in trade, which will stress resilience to shocks, embrace digital opportunities, provide inclusive employment opportunities and build in environmental sustainability.

Public policy can encourage the resilience of small businesses – for example, by providing incentives for economic and trade diversification and subsidizing investments in risk-mitigating technologies. State investments in digital trade facilitation processes and expanded e-payment infrastructure can help reduce exposure to shocks to the cash economy and boost the competitiveness of remote firms.

Regulations can encourage the development of more inclusive and resilient value chains based on contracts that share risk between suppliers and buyers for longer-term, higher-quality stable value chain relationships. Finally, the government can take advantage of the opportunity provided by COVID-19 recovery efforts to 'build back better' in an environmentally sustainable way.

By making it easier for small firms to contribute to sustainable and resilient economic development, these steps can help build a strongly rooted, comfortable and secure life for all Filipinos, as envisioned in *AmBisyon Natin 2040*.

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Chapter 1

Unleashing the potential of small businesses

Unleashing the potential of small businesses

The COVID-19 pandemic is first and foremost a health crisis, and like other countries, the Philippines enforced a lockdown to stop the spread of the virus. However, the halt of economic activities has had a huge impact on small companies.

The pandemic has strongly affected two-thirds of Filipino firms, according to data from the ITC COVID-19 Business Impact Survey. With fewer resources to ride out the storm, small and medium-sized enterprises (SMEs) have been especially vulnerable to the repercussions of the crisis.

This is particularly worrisome given the importance of SMEs to the development and trade of the Philippines. They account for more than 99% of registered businesses in the country and provide 60% of jobs, including for vulnerable groups such as women, youth and rural people.[2] These firms make important contributions to the national economy, adding value worth about 36% of gross domestic product and recording overseas sales that generate a quarter of export revenues.[3]

The emergence of the Philippines as a significant player in the region and the world has opened up new opportunities for its firms. Many small Filipino enterprises are rising to the occasion, acting as a vital conduit that connects global value chains, growth and change to the jobs, products and well-being of ordinary people. Their role in making growth inclusive makes their needs and potential all the more relevant to policymakers interested in sustainable development.

The Philippines boasts a well-developed business ecosystem (Box 1). A comprehensive network of government programmes and policies bolster the international competitiveness of small enterprises. Yet many small firms face persistent challenges as they try to compete. This report identifies those challenges and suggests how policymakers can address them.

Tackling the obstacles that small businesses face on a daily basis is all the more urgent in light of the COVID-19 crisis. With the help of a supportive business environment, Filipino SMEs can become more resilient to shocks, embrace digital opportunities, and promote inclusive and sustainable growth. A competitive, resilient SME sector can help achieve the aspiration outlined in *AmBisyon Natin 2040* of a strongly rooted, comfortable and secure life for all Filipinos.[4]

To set this process in motion, however, leaders need better data about the state of competitiveness in their country. What limits competitiveness and what characteristics make firms more resilient to shocks? What can be done to improve the competitiveness and resilience of SMEs?

To answer these questions, the International Trade Centre (ITC) partnered with the Bureau of Small and Medium Enterprise Development (BSMED), an office of the Department of Trade and Industry of the Philippines, to assess the competitiveness of SMEs and the impact of COVID-19 on Filipino firms.

Under this collaboration, the ITC SME Competitiveness Survey questionnaire was administered to 514 businesses across the Philippines in late 2019. In early 2020, 454 of these respondents also took part in a follow-up interview about the impact of COVID-19 on their businesses. This report presents the findings of both surveys.

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Box 1: Government policies for small and medium-sized enterprises

The government has adopted *AmBisyon Natin 2040* as the long-term vision for the country. The road to achieving this vision is charted in the Philippine Development Plan 2017–2022 and its 10-point socioeconomic agenda, which underscores the role of SMEs in helping to increase competitiveness and make it easier to conduct business.

This is further elaborated in the Micro, Small, and Medium Enterprise Development Plan 2017-2022, including through efforts to streamline business permit and licensing systems; reduce regulatory burdens; strengthen institutional support; and generate and analyse relevant data.

The development plan is aligned with other SME policymaking endeavours in South-East Asia, including the Asia-Pacific Economic Cooperation (APEC) Boracay Action Agenda to Globalize MSMEs; the APEC SME Working Group Strategic Plan 2017-2020; the Association of Southeast Asian Nations (ASEAN) Strategic Action Plan for SME Development 2016-2025; and the Manila call to Action for ASEAN MSMEs.

The Manila call to Action created the 7Ms to MSME Development approach. The Department of Trade and Industry has used this framework to promote mindset, mastery, mentoring, money, machines, markets and models for successful enterprises.

Programmes to achieve these goals are implemented using the legal framework established by the Magna Carta for Micro, Small and Medium Enterprises (MSME), which sets out a consolidated all-of-government approach to SME support. The Magna Carta established the MSME Development Council, which is tasked with crafting SME policy.

Policies are implemented through a network of more than 1,130 Negosyo Centers across the Philippines that act as lynchpins in an integrated set of business support services for SMEs.[5] Companies register, participate in training programmes and obtain marketing information at their local Negosyo Centers. The Shared Service Facility (SSF) Programme provides machinery and equipment for shared use in priority industry clusters in selected regions.[6] The Retail Lending Program and Pondo sa Pagbabago at Pag-asenso (P3) Program and the Export Pathways Program both provide additional targeted assistance.

Assessing competitiveness

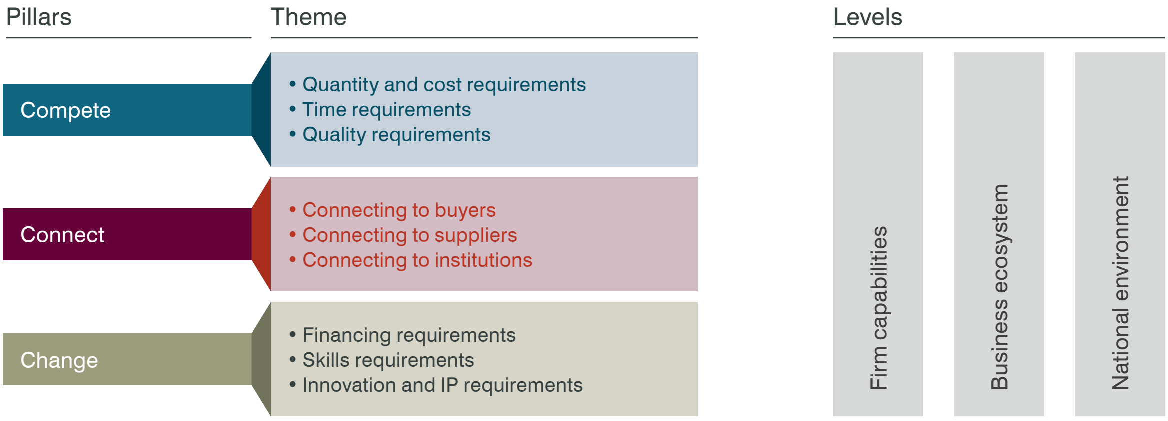
The International Trade Centre (ITC) developed the SME Competitiveness Survey[7] (SMECS) to help countries collect the data needed to measure the competitiveness of their enterprises. As of June 2020, more than 17,000 firms had been surveyed in 46 countries, including Cambodia, Indonesia, Myanmar and Sri Lanka.

The tool is designed to combine information at the meso (local support ecosystem for businesses) and micro (firm capacity) levels to provide a nuanced picture of the capacity of a country's private sector to compete in international markets and be more resilient to shocks.

Small and medium-sized enterprises are defined as firms with fewer than 100 employees (see Appendix). The term 'SME' thus includes microenterprises. Although the focus is on small and medium-sized enterprises, some large companies are included in the survey so the competitiveness of SMEs and large firms can be compared.

The importance of competitiveness in driving firm survival, growth and trade make it a central element in economic development. For this reason, ITC has developed an analytical framework to understand firm competitiveness and how it can be improved over time. The framework is built around three pillars that drive the capacity of a company to be competitive across three levels of the economy (Figure 1).[8]

Figure 1 The SME Competitiveness Grid



Source: ITC.

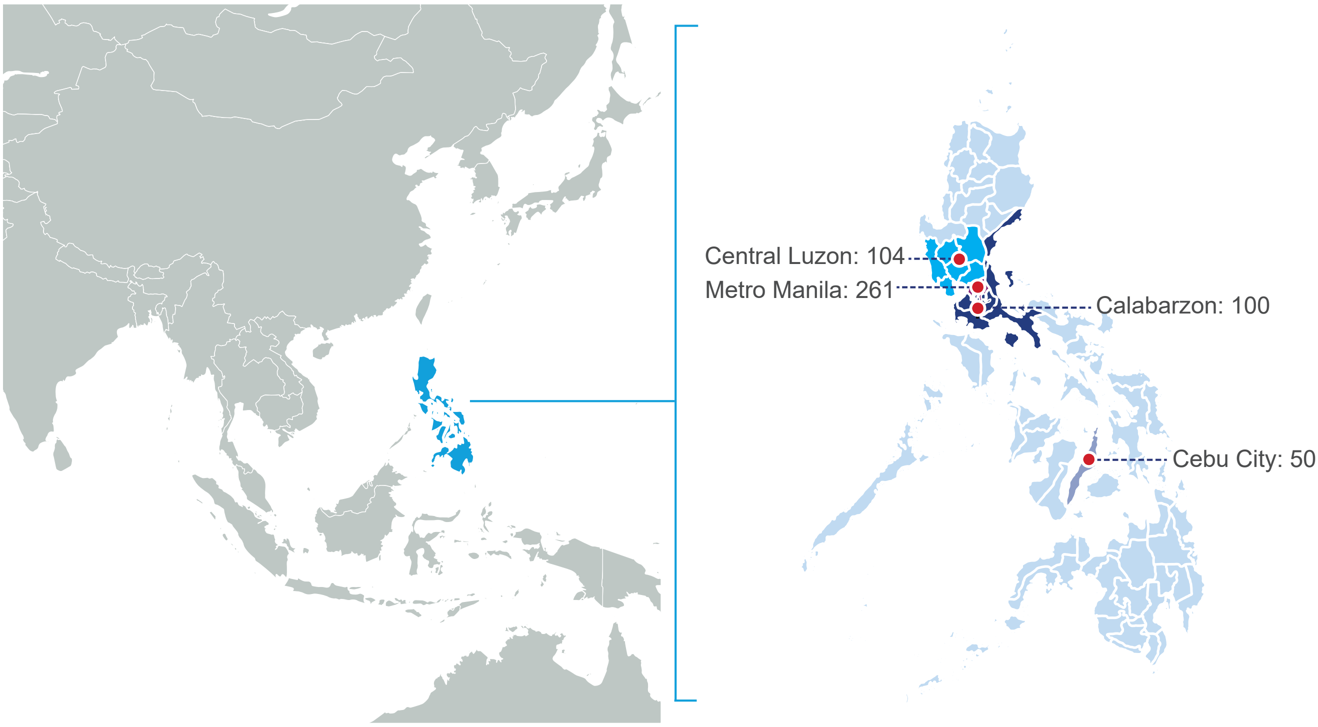
The SME Competitiveness Survey in the Philippines

ITC implemented the SME Competitiveness Survey in the Philippines in partnership with BSMED, which provided guidance and direction. SMART Research Philippines, a local data collection company, conducted the surveys.

To facilitate the collection of data, a sample of firms was randomly selected from across the country. The sample was spread across regional districts, sectors (primary, manufacturing and services) and size (micro, small, medium-sized and large). Data were to be collected on firms operating in the primary (i.e. agriculture and mining), manufacturing and services sectors from four key regions. To the extent possible, the sample in each region was to be composed of exporting and non-exporting firms.

SMART Research surveyed 514 enterprises in November–December 2019 using the SME Competitiveness Survey questionnaire. Data were collected from four different regions of the country: the National Capital Region (also known as Metro Manila), Calabarzon, Central Luzon and Cebu City. Figure 2 highlights the surveyed regions.

Figure 2 Surveyed regions of the Philippines



Source: ITC based on SME competitiveness data collected in the Philippines.

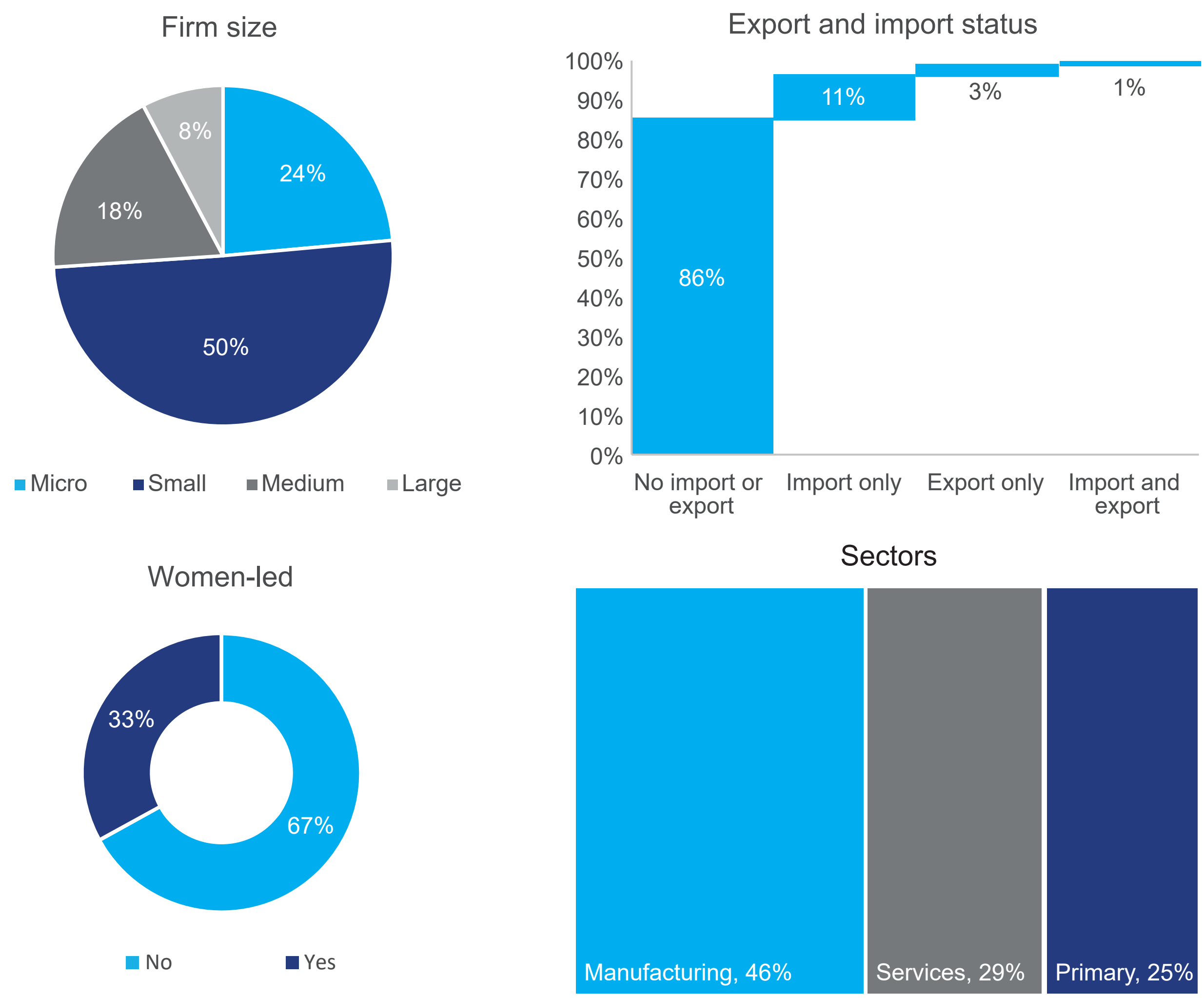
Box 2: About BSMED and ITC

BSMED is the office responsible for implementing SME policy in the Department of Trade and Industry of the Philippines. As the body responsible for coordinating the implementation of the MSME Development Plan, and as the secretariat of the MSME Development Council (Box 1), it supports policies and programmes for SME development in the country. It also prepares briefing documents, reports and position papers for the council, and convenes an annual MSME week.

ITC was created in Geneva, Switzerland, as a joint agency of the United Nations and the World Trade Organization dedicated to strengthening the competitiveness of small and medium-sized enterprises to build vibrant, sustainable export sectors that provide entrepreneurial opportunities, particularly for women, young people and poor communities.

Figure 3 showcases basic information about the enterprises that were interviewed. Small and medium-sized enterprises comprise 92% of the sample. Almost half of the participating companies are active in the manufacturing sector, with the remainder split between the services and agricultural sectors.

Figure 3 Characteristics of companies that participated in the survey



Note: Micro-sized firms are defined as those with four or fewer employees; small firms have 5–19 employees; medium-sized ones have 20–99 employees; and large firms have 100 or more employees. This definition is different from the legal definition in the Philippines (see Appendix subsection on 'What are SMEs'). Women-led firms are managed by a woman and at least 30% owned by women.

Source: ITC calculation based on SME competitiveness data collected in the Philippines.

About 15% of respondents were involved in international trade either as exporters or importers. Women led one in three companies, indicating that female entrepreneurship is an important part of the Filipino economy.

About 91% of the surveyed enterprises said they were registered with or licensed by a national authority. Yet the latest labour force survey figures show that the informal sector employs 38% of the labour force.[9] With most informal companies employing fewer than 100 people, they make up a significant share of SMEs in the country.

As these firms employ more people, become competitive and grow, they contribute to the economy, become formalized, and can make important contributions to Filipino development. However, they can be hard to reach. As just

9% of the surveyed firms are informal, the current analysis cannot cover them fully; rather, the study focuses on the formal sector.

The ITC COVID-19 Business Impact Survey in the Philippines

In reaction to the spread of the pandemic, the Filipino government declared a state of calamity on 16 March 2020 and imposed an enhanced community quarantine (ECQ) across the whole of Luzon Island. With businesses shut down – except for those that provide food, healthcare, banking or business process outsourcing services, or export-oriented industries – many SMEs were put in dire straits.[10]

Companies were struggling with this situation mere months after being interviewed for the SME Competitiveness Survey at the end of 2019. Yet it became rapidly apparent that COVID-19 was a game changer that threatened to remake the private sector landscape in the Philippines. This is why ITC and BSMED renewed their partnership in early 2020 to collect data on how COVID-19 was affecting small businesses.

In April and May, 454 of the firms that were interviewed for the SMECS participated in the ITC COVID-19 Business Impact Survey. SMART Research conducted the survey, this time by telephone.

This report presents the results of that survey alongside findings on competitiveness. They show the extent and distribution of the impacts of the lockdown on Filipino businesses, as well as the nature of help that is needed. In this sense, they are useful for policymakers looking to invest scarce government resources in the short-term help that is most urgent.

The data from both surveys are useful for another reason. We live in disruptive times, where the threat of climate crisis, trade war, technology shift and political upheaval threaten to change the business landscape regularly. If small Filipino firms are to survive and thrive despite this turmoil, we must know more about how to help them through rocky waters.

Experience has shown that when a crisis hits, some companies are more exposed to the shock than others, and so are more affected. Although there is little they can do about their exposure in the short run, they are protagonists in the story of how they cope with crisis. Company management takes decisions about strategies to cope that determine whether they are resilient to the storm.

The exposure of a firm to the shock, along with its coping strategies, combine with the information and benefits it receives to deliver outcomes: will the business be engulfed by the crisis and succumb to bankruptcy? Or will it survive in a weaker, or even stronger, state?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Analysis of the data from the two surveys reveals that company competitiveness is closely linked to its experience of crises. The pandemic had a milder impact on firms with stronger performance along certain competitiveness characteristics.

In particular, the capacity to compete in the short run seems to have reduced exposure to the shock. The capacity to change made it easier to adopt positive coping strategies, and the capacity to connect enabled companies to access information and benefits.

If Filipino SMEs are to be made resilient to the next crisis, each of these competitiveness characteristics needs to be better understood and improved.

The rest of this report presents the survey findings in the Philippines. This empirical evidence can be a useful tool for stakeholders working to boost SME competitiveness and resilience.


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OPENING PROGRAMME
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Chapter 2

Capacity to compete reduces exposure to shocks

Capacity to compete reduces exposure to shocks

Being able to make a product that customers want at a reasonable cost is at the centre of a company's value proposition – and its ability to compete on local and international markets. The ability of the firm to be productive, deliver on time and obtain necessary quality certificates all indicate its ability to meet market requirements through its daily operations.

Management capacities at the firm level as well as the business ecosystem in which they operate influence this capacity to compete. Empirical evidence from the SME competitiveness survey indicates that most small and medium-sized Filipino firms excel at delivering the right product at the right time.

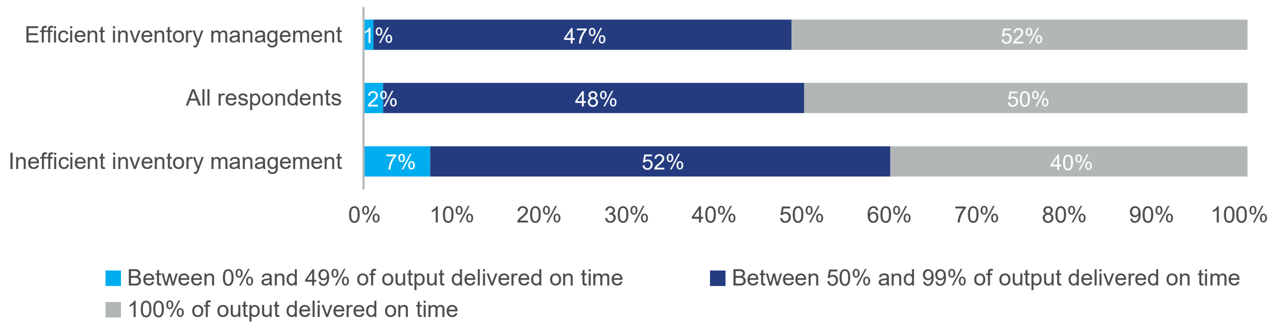
Management skills affect supply-side capacity

Companies that can make more from their inputs are highly productive and often more competitive and profitable as a result. They are able to earn more money on a larger amount of output, given their costs.[11] In the Philippines, interviewed companies produce on average 68% of their maximum possible output.

Filipino firms are also punctual, with half of respondents saying they deliver all of their output on time. Inventory management systems were described as highly efficient by 44% of interviewed companies. Strong performance on quantity and cost requirements can be attributed in part to strong entrepreneurial spirit and capabilities in the country.[12]

The connection between management and timeliness is clear: companies with good inventory management practices delivered more of their output on time. Those that described their inventory management as efficient were 12 percentage points more likely to deliver all their output on time, and were less likely to deliver under half their output on time (Figure 4).

Figure 4 Most goods are delivered on time



Note: Survey asked: 'In the last year, what percentage of this company's goods or services were delivered on time?'
Source: ITC calculation based on SME competitiveness data collected in the Philippines.

This indicates that Filipino companies with stronger management skills (here expressed as the ability to organize the flow of inputs and outputs within the company) are more capable of supplying according to market requirements, including timely delivery. Small enterprises are increasingly using technologies to manage this inventory management task, with 83% using some sort of technology for this purpose and 23.5% making extensive use of related tools.[13]

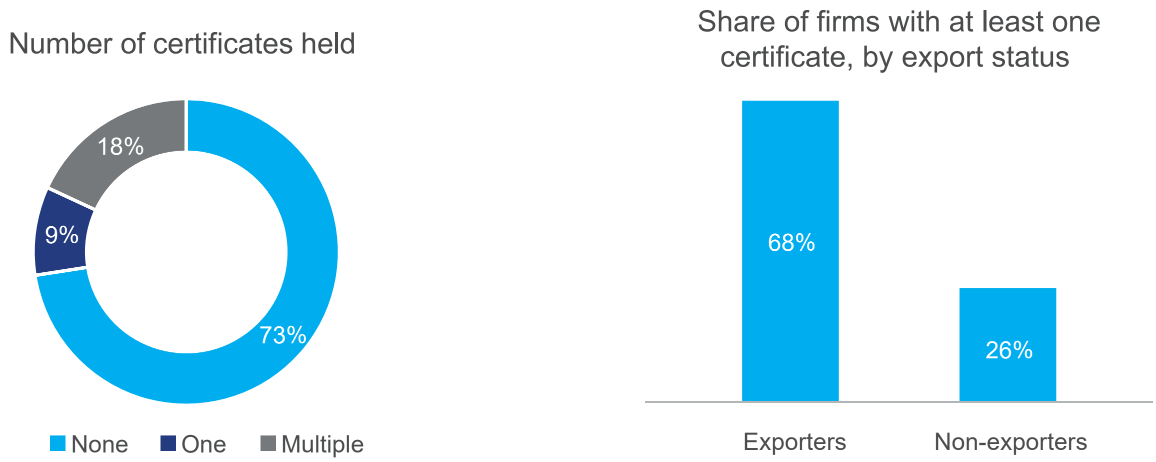
Quality is a must for further upgrades

The Philippines has made great strides in upgrading the terms of its engagement in global value chains in recent decades. For instance, the country has taken on value chain activities (such as assembly or coordination) that used to be carried out elsewhere in East and Southeast Asia.[14]

Upgrading the quality of Filipino output is necessary to continue this trend. Research elsewhere suggests that companies that get certified to international standards can increase their sales to foreign buyers,[15] although the compliance process can be costly.[16]

Just over a quarter of interviewed companies are certified to international standards (see Figure 5). In many cases, certification is part of a strategy for going global. Indeed, 68% of interviewed exporters were certified to an international standard.

Figure 5 Only 27% of firms have an international certificate



Note: Survey asked: 'Does this establishment's main product or service hold any of the following types of internationally recognized certificates?' Options included safety, quality or performance, sustainability, or other certificates. Respondents were included in the exporter category of buyer-connected firms if they gave a positive response to the question 'In the last full calendar year, what percentage of this establishment's sales were direct exports (e.g. products or services exported by this establishment?'

Source: ITC calculation based on SME competitiveness data collected in the Philippines.

The relationship is not so simple as to suggest that certification is necessary for export. Six exporters were thriving despite not holding any international certificate, highlighting that there may be a 'low road' of engagement in international value chains.

Perhaps more surprisingly, 128 companies that supplied exclusively for domestic markets were certified to international standards. This indicates that Filipino firms are picking up international standards to signal their quality to domestic customers. In some cases, this is a 'pull' reaction: companies whose buyer required them to adhere to standards were much more likely to adopt an international standard.

Yet 51 companies were certified despite no buyer requirement and no export markets, indicating that they are adopting strategically for market positioning reasons. Indeed, these businesses were more likely to say they were competing by offering high-quality goods and services. By choosing to adopt standards, these companies are improving the overall quality competitiveness of Filipino firms and bettering the country's long-term prospects in the global economy.

However, attitudes about quality upgrading depend on firm characteristics. Larger companies and services providers are more inclined to get certified. Just 20% of companies in the primary sector have adopted international standards.

The certification scheme of choice also varies, with safety and quality standards appearing most popular among Filipino firms. The most popular domestic schemes were those offered by the Department of Trade and Industry as well as the fire and safety inspection certificate.

Late payments hurt cash flow of small firms

Although the evidence suggests that Filipino firms often deliver on time, many buyers do not pick up and pay for their order on time. As one women-led manufacturer of clothing in Cebu City put it: 'There are many orders unclaimed. We cannot do anything except to wait for the clients to claim it even if it takes a month, or a year. In that case, it means a big loss for our capital to revolve.'

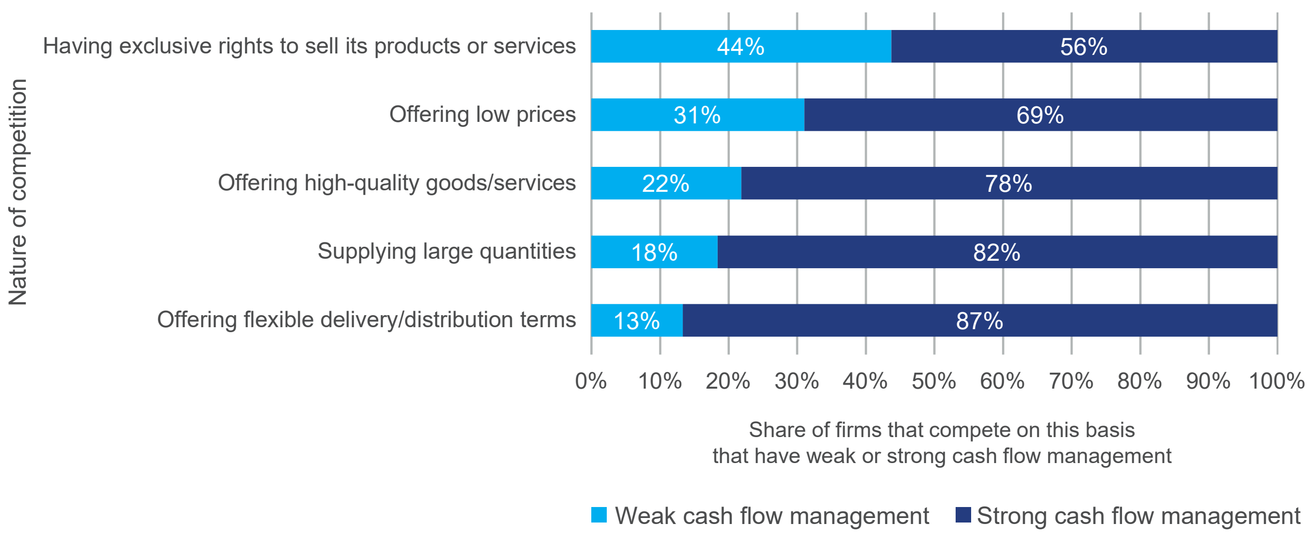
Some companies can manage their finances to cover the period of fabrication, storage, delivery and final payment. Indeed, 50% of survey respondents said they had a 'very good ability' to manage cash flows for this purpose. However, that was not the case for all firms. For example, 11% of manufacturers said cash flow problems were their biggest challenge in meeting market requirements.

Cash flow practices greatly influence how an enterprise engages with markets. Analysis of the SME Competitiveness Survey data from the Philippines indicates that having stronger cash flow management makes it more likely that the firm can compete on remunerative grounds, for example, by supplying large quantities, flexible delivery terms and better-quality products.

When a company can afford to produce large quantities, it can supply to larger buyers who make regular orders, thereby stabilizing revenues and reducing the high transaction costs associated with small, non-repetitive orders. Competing by offering better-quality products also opens up the possibility of earning higher prices associated with quality premiums, along with access to elite niche markets.

These methods are less common among firms with weak ability to manage their cash flow. They are more likely to compete on shaky, non-remunerative grounds – for example, by offering low prices or being the only convenience shop in town (Figure 6). Their cash flow issues seem to prevent them from investing in remunerative market strategies.

Figure 6 Managing cash flow boosts nature of competition



Note: Survey asked: 'Which statement best describes this establishment? This establishment competes by', with the list of types of competition shown in the figure; and 'Please rate this company's ability to manage its cash flow to reliably execute payments.' The figure show what percentage of firms choosing a specific type of competition said about their cash flow management, defined by their choice of options 5 or 6 on a likert scale ranging from 1 (no ability to manage cash flow) to 6 (very good ability to manage cash flow).

Source: ITC calculation based on SME competitiveness data collected in the Philippines.

The Asian Institute of Management confirms that it can be counterproductive for Filipino companies to respond to tight competition by cutting prices or costs, because doing so reduces revenues and quality, which ultimately hurts the health of the firm. Older and bigger firms are more likely to respond to tight competition in ways that underpin growth, such as product improvements.[17]

Cash flow struggles seem to cripple the ability of companies to grow. Micro and small firms tended to rate their ability to manage cash flow more poorly, suggesting there is a vicious circle: small companies can't manage short-term capital crises, which keeps them from allocating capital to growth, which in turn reduces their ability to manage short-term cash flow issues.

Cash flow problems are forcing small Filipino firms to compete in counterproductive ways that hamper their growth. Policies to encourage timely payment of bills could help address this issue, for example, through public procurement or contract law enforcement rules that incentivize punctual payments for SME goods and services.

Better access to short-term financing for working capital could also help. One entrepreneur said: 'There are instances where I need to use my personal savings to sustain my business and cover the rental costs. I usually seek financial help from my relatives as well.'

However, there seems to be little appetite or aptitude for SME access to bank loans. Just 26% of interviewed firms said they needed a loan, a much lower rate than in other countries where the SME Competitiveness Survey was conducted. This is consistent with evidence on relatively low levels of financial intermediation in the Philippines: domestic credit to the private sector was just 44.7% of gross domestic product in 2016.[18]

Furthermore, loans are often only given to companies that have a bank account. Only 35% of Filipinos over 15 years of age have a bank account. Smaller firms interviewed for the SME Competitiveness Survey were less likely to have a bank account than larger firms. Yet companies that have a bank account have significantly better cash flow management.

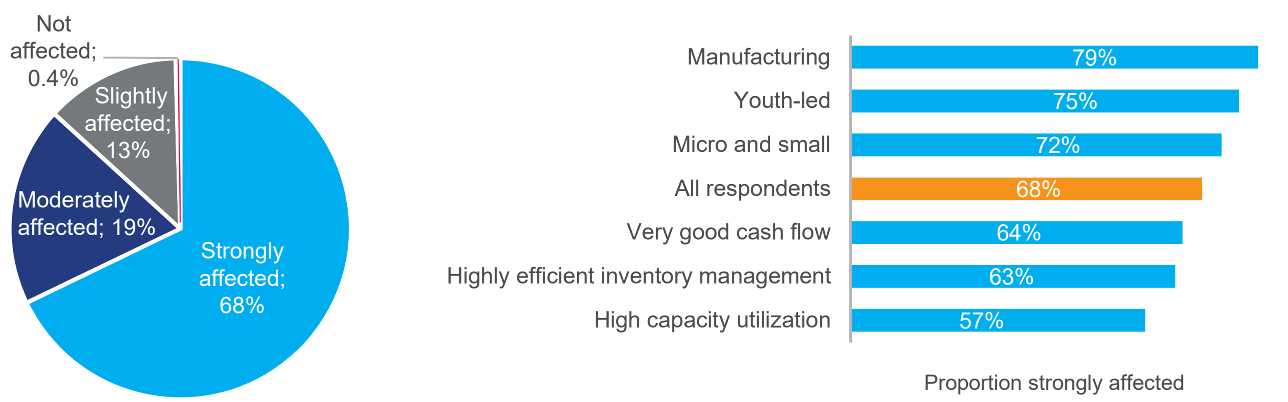
By encouraging the establishment of bank accounts, improved financial inclusion in the Philippines could encourage both access to credit and cash flow management. These are important in their own right but are also integral to the ability of SMEs to compete on remunerative grounds in the marketplace.

Pandemic was less severe for competitive firms

It is easier for companies with a strong business plan and a track record of meeting market requirements to stop their businesses temporarily and then restart them after the crisis ends. That is, the ability to compete successfully reduces the exposure and sensitivity of a company to shocks.

Evidence from the ITC COVID-19 Business Impact Survey shows that the pandemic has affected 99% of Filipino businesses. What's more, 68% of interviewed firms said they had been strongly affected (Figure 7). Companies that were smaller or led by youth, and those involved in international trade, were more likely to be strongly affected.

Figure 7 COVID-19 strongly affects 68% of firms



Note: Survey asked: 'How have your business operations been affected by the coronavirus (COVID-19) pandemic?'

Source: ITC calculation based on SME Competitiveness Survey and ITC COVID-19 Business Impact Survey data collected in the Philippines.

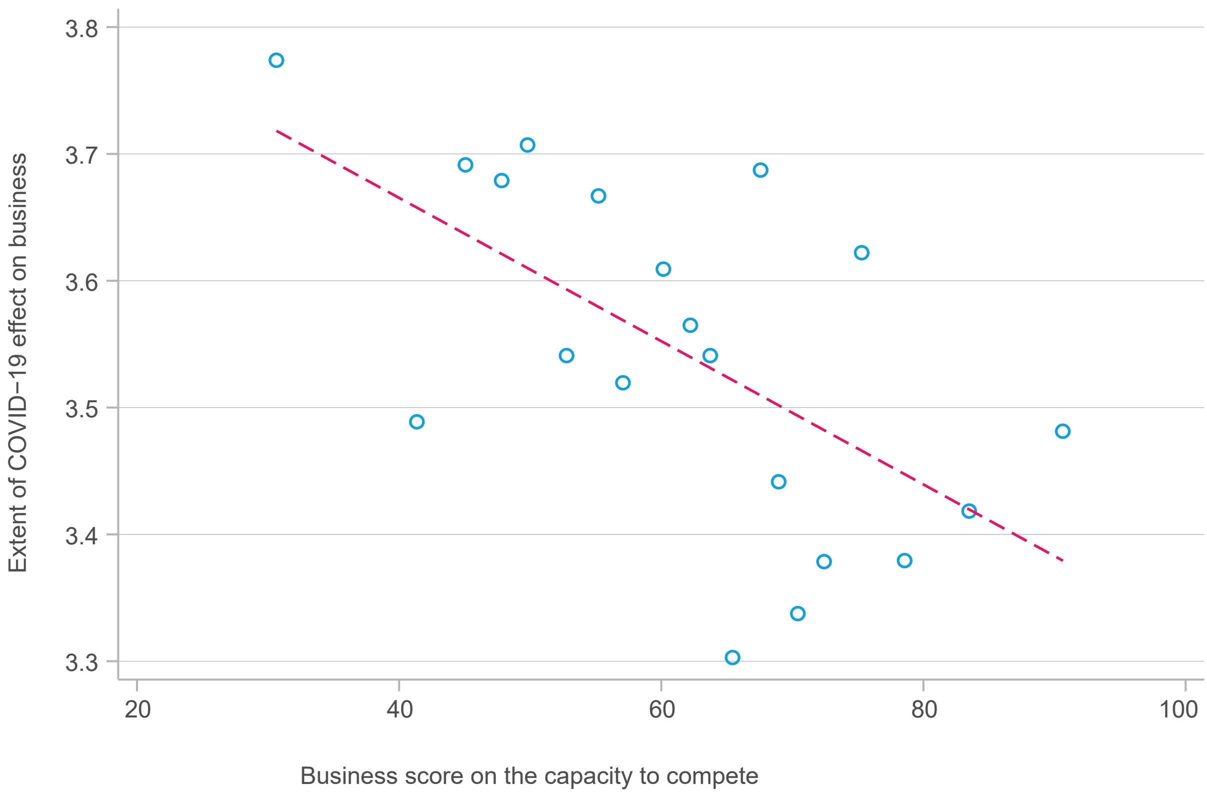
Interestingly, the evidence indicates that firms with a greater capacity to compete before the pandemic were less likely to be strongly affected by it. Just 64% of companies with very good cash flow, 63% of companies that described their inventory management as 'highly efficient', and 57% of those with full capacity utilization described themselves as strongly affected, compared to 68% of all respondents in the sample (Figure 7).

Competitiveness is about making something people want to buy – and earning a decent profit from it. It happens when a firm has its cost, production, management and quality processes in order. Based on the competitiveness survey responses, ITC computed a 'capacity to compete' score for each firm and found that those with a higher competitiveness score were less likely to be strongly affected by the pandemic (Figure 8).

Manufacturers have generally been hit harder than companies in other sectors, but not because they are less competitive. Four in five interviewed industrial companies said they had been strongly affected, compared to just half of primary firms. This is because while the temporary shutdown in the Philippines affected all companies, manufacturing firms also had to cope with the disruptive effects of overseas lockdowns on international manufacturing supply chains.

ITC analysis estimated that Filipino manufacturing exports fell by $2.4 billion in the first half of 2020 due to lower sales of intermediary inputs into international supply chains amid a two-month long factory shutdown in all partner countries.[19] Less demand for Chinese manufacturing inputs caused about a third of the total projected export decline.

Figure 8 Firms with more capacity to compete were less affected by COVID-19



Note: The relationship between the two variables is the result of a binned scatterplot. The survey asked: 'How have your business operations been affected by the coronavirus (COVID-19) pandemic?' Answers ranged from 1 (not affected) to 2 (slightly affected), 3 (moderately affected) to 4 (strongly affected). The answers to several questions discussed in this section were used to calculate firm score on their capacity to compete.

Source: ITC calculation based on SME Competitiveness Survey and ITC COVID-19 Business Impact Survey data collected in the Philippines.

The drop in manufacturing trade is having ripple effects across the Filipino manufacturing sector, as exporters stop sourcing inputs from local suppliers and local manufacturers struggle to obtain imported inputs.

The measures taken to address the health emergency have struck at the heart of companies' balance sheets across the country, survey evidence indicates. Sales in January–April 2020 were lower for 88% of interviewees compared with a year earlier. Smaller firms, manufacturers and/or companies that trade were more likely to report lower sales. A similar percentage of firms reported difficulty accessing inputs.

The pandemic has profoundly altered the business ecosystem in which companies operate. Almost half (46%) of Filipino firms that responded to the ITC COVID-19 Business Impact Survey said their access to logistics services was reduced. Liquidity crises in households and businesses in the rest of the economy had knock-on effects, too: a third of firms said their clients were not paying their bills.

Other common effects of the crisis included reduced investment (reported by 28% of respondents); new problems with infrastructure (14%) and fewer certification services (10%). Companies also thought the international trading environment had become more tumultuous. The share of firms saying that trading overseas is more uncertain now than five years ago tripled, from 11% before COVID-19 to 32% during the pandemic.

Policy insights: Easing short-term cash flow issues for competitiveness and crises

Many small Filipino companies have been strongly affected by measures taken to contain the spread of COVID-19. Smaller companies, those led by youth and those in the manufacturing sector have been more exposed to the shock, particularly if the management of the firm was weaker ex ante.

In fact, even before the crisis hit, these firms suffered from cash flow issues because of delayed payments. Policy measures are needed to encourage timely payment on orders. A deliberate look at government public procurement plans, and specifically their provisions for timely payment and reservations to SMEs, could help tackle this issue. Improving the judicial remedies for contracts that have gone unpaid could also prove worthwhile.

Once COVID-19 hit, the drop in sales and payments immediately threatened the bottom line of firms that were already weak because of poor cash flow management or other factors. The survey evidence confirms the liquidity crisis that accompanies lockdown measures. Filipino companies that participated in the COVID-19 business survey said that tax waivers, temporary tax breaks and cash transfers would be the most helpful government measures.

ITC's 15-point action plan for supporting small businesses during the COVID-19 crisis and beyond points out that, in the short run, programmes are needed to expand and facilitate access to finance for SMEs, including those run by women or young entrepreneurs.

The Philippine government has taken action to create a financial buffer to address short-term liquidity issues. In the long term, however, the Philippines faces new global trends as well as other potential crises.

Digital technologies, already flourishing before the pandemic hit, became essential. Businesses operating online were able to avoid the full effect of the pandemic as consumers shifted to electronic commerce. Government policy can support small business use of digital technologies to reduce their exposure to future crises. Investments in expanded e-payment infrastructure, for example, can help reduce exposure to shocks to the cash economy and boost the competitiveness of remote firms.[20]

The Department of Trade and Industry organized a series of free webinars during the ECQ aimed at helping SMEs learn about taking their businesses online. Continued efforts to facilitate equitable access to the digital transition will ensure that Filipino growth is both inclusive and resilient to crisis.

Chapter 3

Adaptability underpins resilience to crisis

Adaptability underpins resilience to crisis

Today's rapidly shifting marketplace means companies must be able to change in response to dynamic market forces. When firms can mobilize financial resources and employee skills and invest them in innovation, they stay afoot with the latest market demands and can expand their market share.

The ability to continuously transform knowledge and ideas into new products, processes and systems is essential to a company's capacity to change.[21] Such innovation is all the more important today, as the knowledge economy increases the pace and economic value of knowledge-intensive parts of global value chains.

Being able to innovate is particularly important for SMEs that must stay current with rapid advances in new technologies used in global value chains, so they seek out a workforce ready for the challenge.[22] Small companies need skilled workers with appropriate education and training if they are to innovate as they enter more knowledge-intensive activities.

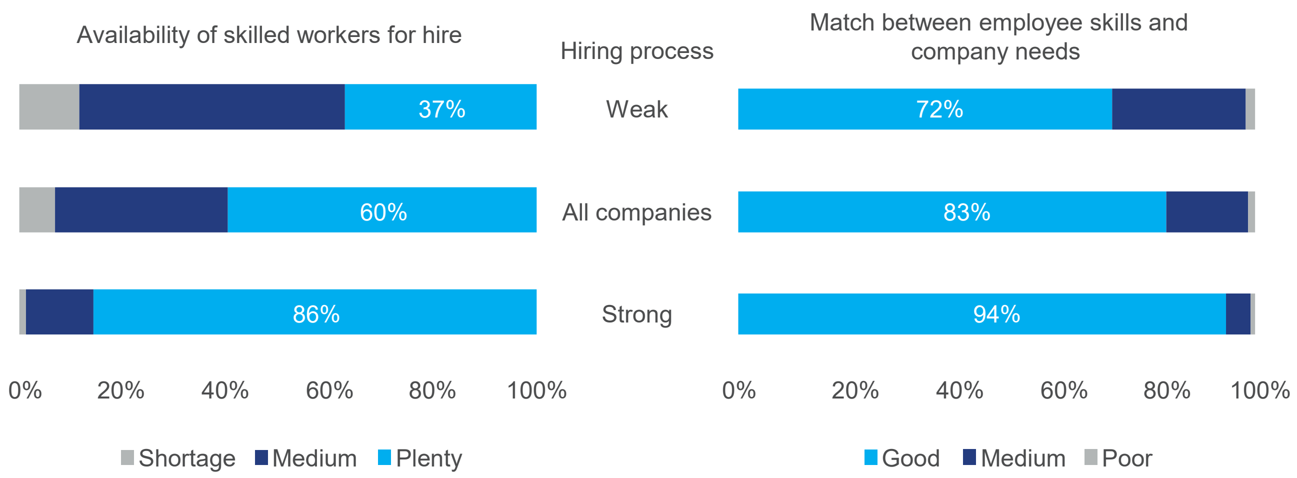
The availability of a talented local workforce not only helps predict productivity, but also a country's ability to export[23] and diversify the goods and services it sells overseas.[24] The availability of skills affects the capacity to innovate and access more lucrative business activities. Evidence shows that firms in countries with relatively high skill levels typically carry out relatively high-skill-intensive and more profitable tasks in global value chains.[25]

Most firms find skills that match their needs

The Philippines has made good progress in increasing the skills of its citizens. In 2017, lawmakers passed the Republic Act, which set free tuition for students at universities, colleges and vocational training institutions.[26] Along with the current administration's latest education plans, this reflects a strategic aim of upskilling the labour force in the near term.[27]

These investments in human capital are apparent in the survey results, which showed most firms were able to find the skill sets needed for their business. Most (60%) said plenty of skilled workers were available for hire. Even more (83%) said there was a good match between the skill sets of current workers and the needs of the company. Survey results reveal that firms with stronger hiring processes tend to have a better match between the skills of their employees and their firm needs (Figure 9).

Figure 9 Strong hiring practices bring in needed labour skills



Note: Survey participants were asked to 'please rate the extent to which the skill set of currently employed workers matches the needs of this company' and 'please rate availability of skilled workers for hire'. Response options ranged from 1 (poor) to 6 (strong): answers of 1 or 2 were put in the worst category, 3 or 4 in the middle category, and 5 or 6 in the best category.

Source: ITC calculation based on SME Competitiveness data collected in the Philippines.

This shows that labour market success stems in part from a firm's own activities. Besides creating strong hiring processes to find suitably skilled workers, Filipino SMEs incur about 10% of their costs in training.[28] This indicates that companies are also using in-firm training programmes to tackle skill shortages in the labour force.

Business ecosystem factors also help explain whether firms are able to access suitable candidates. Survey results suggest that companies that are able to find institutions with high-quality skills training programmes are more successful in matching employee skills to company needs. Furthermore, lower-cost programmes that teach skills may make it easier for businesses to recruit the most suitable candidates for job openings.

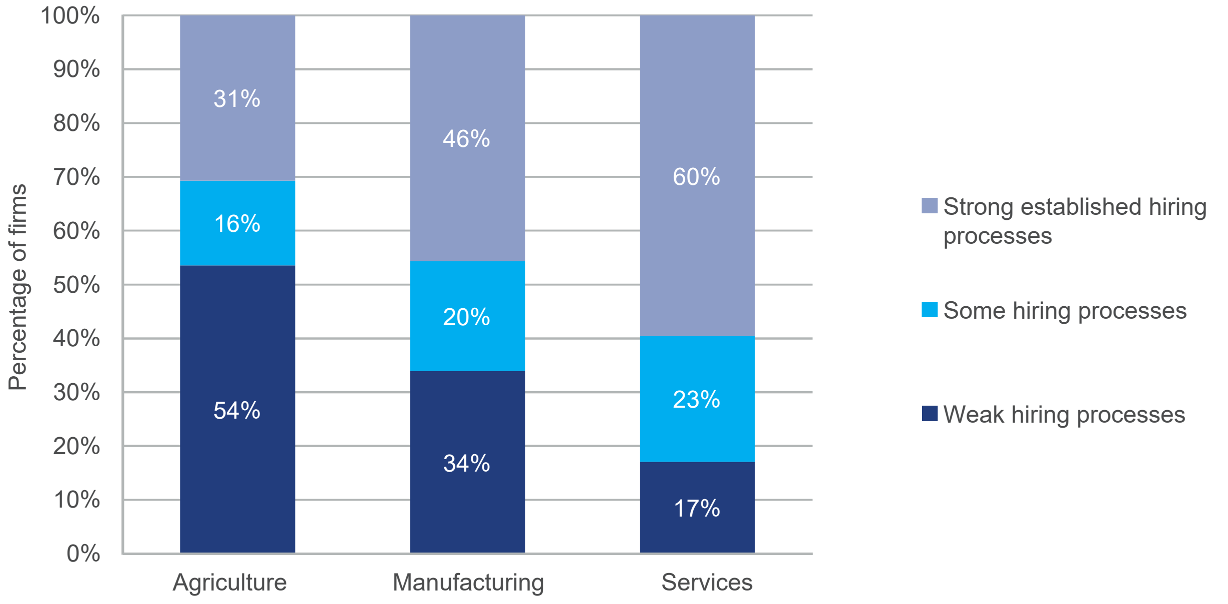
Although most Filipino companies usually manage to access the skills they need to compete, some types of firms are clearly struggling to do so. Small enterprises report significantly worse matching rates between their needs and the skills of their workforce than larger firms.

Notably, just 49% of youth-led firms can find enough skilled workers, compared to 60% of firms led by their elders. This may be due to faulty human resources management – half of youth-led firms lack an established hiring process, for instance.

Enterprises in the agricultural sector have a hard time finding workers. As Figure 10 illustrates, 60% of service firms and 46% of manufacturers had strong established hiring processes, while just 31% of agricultural firms could say the same.

Agricultural firms seem to benefit less from the skills provided by their business ecosystem. For example, they struggle more than their peers in manufacturing and services to access high-quality skills training programmes. Survey results indicate that only 45% of agriculture firms access high-quality programmes, compared with more than half of manufacturing firms and two-thirds of service firms.

Figure 10 Agricultural enterprises are weak on hiring



Note: Respondents were asked to 'please rate the extent to which your company has an established hiring process to hire the best candidates'. Response options ranged from 1 (no established process) to 6 (strong established process). Responses of 1 and 2 were deemed 'weak hiring processes', 3 and 4 as 'some hiring processes' and 5 and 6 as 'strong established hiring processes'.

Source: ITC calculation based on SME competitiveness data collected in the Philippines.

Having good hiring practices is valuable for its own sake, but also has knock-on benefits on the ability to innovate. The evidence above suggests that firms with better hiring practices tend to build up a set of employees whose skill set better matches the needs of the company. This is crucial, as analysis of the survey data further indicates that companies with a good skills match are significantly more likely to say they often develop and apply new or improved processes or products.

In sum, strengthening hiring processes improves skills, which fosters innovative activity. This is essential for competitiveness and resilience, as discussed below.

Strong innovation across the economy

Evidence from the competitiveness survey underscores that high rates of innovation can be found throughout the private sector. Two-thirds of interviewees said they frequently develop and implement new or improved processes and goods.

In some cases, these innovations resulted from formal investments in research and development (R&D) and led to intellectual property protection. Serious resources were dedicated to R&D creation in 58% of surveyed firms, and

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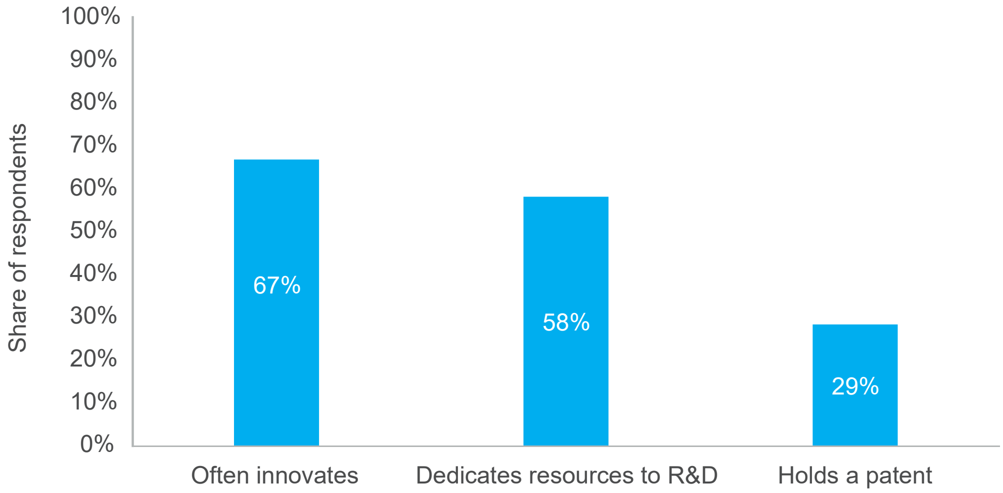
Figure 11 Most firms innovate and conduct research



Note: Respondents were asked to 'please rate the frequency with which your company develops and implements new or improved processes or products', 'please estimate the level of resources your company commits to research and development', and 'Does this company have a registered patent?' Responses to the first two questions are considered a 'yes' if the respondent chose options 4, 5 or 6 on a likert scale ranging from 1 (rarely or no resources respectively) to 6 (often or high level of resources respectively).

Source: ITC calculation based on SME competitiveness data in the Philippines.

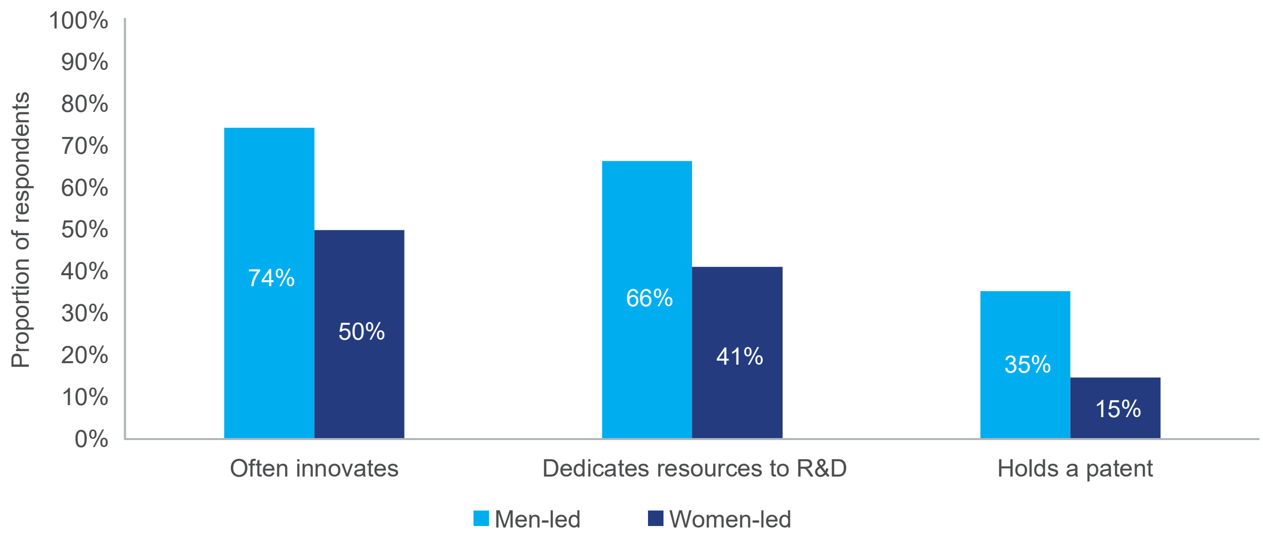
29% held a patent (Figure 11).The interregional distribution of innovation follows the pattern noted elsewhere in the report, with Calabarzon scoring highly on all measures. Businesses in the National Capital Region and Calabarzon gave their innovation-supporting institutions the highest quality ratings, while those in Cebu and Calabarzon dedicated the most resources to R&D.

Data from the SMECS indicate that innovation is most common among firms in the paper manufacture, retail, food product manufacturing and metal product subsectors of the Filipino economy. Indeed, four-fifths of paper and paper product manufacturers said they often developed new or improved goods or processes. The service sector has a higher rate of innovation – defined as the frequency of creating new products and processes – than the manufacturing or agricultural sectors.

Analysis of survey data also show that entrepreneurial characteristics affect the capacity to change. Women-led companies tend to dedicate fewer resources to innovation, so they developed few new goods or processes (Figure 12). Youth-led, micro and small companies also perform relatively poorly on innovation.

This is problematic, because it indicates that firms led by women or youth and smaller enterprises are not investing in expansion, growth, innovation and change. Support is needed to change this situation if disadvantaged firms are to grow.

Figure 12 Businesswomen innovate less than businessmen



Note: Respondents were asked to 'please rate the frequency with which your company develops and implements new or improved processes or products', 'please estimate the level of resources your company commits to research and development', and 'Does this company have a registered patent?' Responses to the first two questions are considered a 'yes' if the respondent chose options 4, 5 or 6 on a likert scale ranging from 1 (rarely or no resources respectively) to 6 (often or high level of resources respectively). A company is defined as 'women-led' if it is managed by a woman and at least 30% owned by women.

Source: ITC calculation based on SME competitiveness data collected in the Philippines.

Adaptable firms better withstood pandemic

A company's ability to change using skills, financing and innovation underscores its ability to shift with market trends. This adaptive capacity is essential to building resilience to crises such as the COVID-19 pandemic. That is because enterprises that already have the tools and habit of changing often have the skills, creativity and funds on hand to survive.

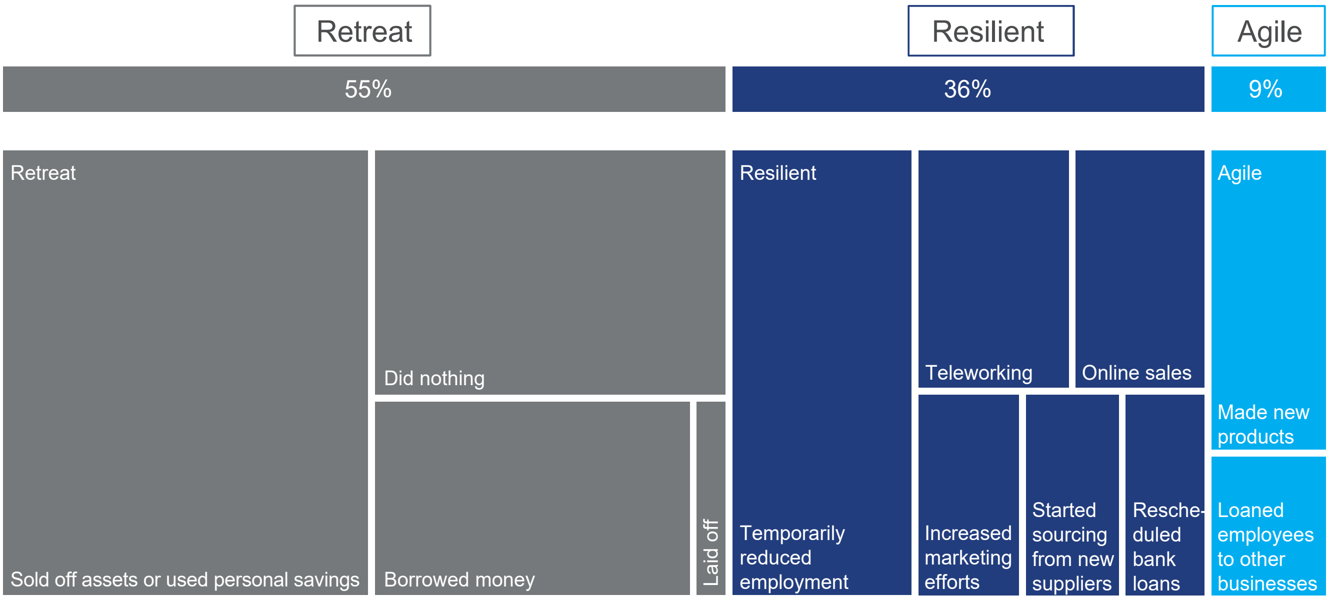
Participation in the knowledge economy helped many Filipino firms cope with COVID-19. Although companies could not do much about how they were exposed to the effects of the ECQ, they could – and did – decide what to do about it. Four of five surveyed enterprises adopted at least one strategy to deal with the crisis.

The most common responses were to use personal savings or sell off assets, temporarily reduce employment and shift to teleworking. Although these techniques may appear to be equal in merit, they actually entail very different approaches to responding to the crisis.

Some of the strategies are relatively better for the long-term health of the enterprise than others. These positive coping strategies help ensure that a business can weather the storm and be in as good shape as before, or become even stronger.

Resilient companies got through the pandemic with their basic form intact. Once the lockdown was imposed, they adopted strategies such as shifting the sales mix towards online channels, sourcing from new suppliers or learning to telework. Although more than half of the enterprises that responded to the ITC COVID-19 Business Impact Survey adopted retreating strategies, 36% of interviewees took a resilient approach (Figure 13).

Figure 13 A third of Filipino firms responded resiliently to COVID-19



Note: The survey asked: 'Have you adopted any of the following strategies to cope with the crisis?' Categorizations: Agile – customized/created new products or loaned employees to other enterprises. Retreat – filed for bankruptcy, laid off employees, sold off assets/used savings, took on new debt or took no action. Resilient – didn't follow a retreat or agile strategies; chose one or more options: temporarily reduced employment; teleworking; rescheduled bank loans; greater marketing; online sales; sourcing from new suppliers; or temporary shutdown.

Source: ITC calculation based on ITC COVID-19 Business Impact Survey data collected in the Philippines.

Some companies have a turbo-charged adaptive capacity that incites them to take advantage of the turmoil brought on by a new situation. Firms that adopt agile strategies transform in response to circumstances, however new they are. During the pandemic, agile Filipino companies created new goods and services such as designer masks and rapid testing technologies.

When lockdowns prevented them from opening, they lent their employees to other businesses in essential industries. This approach can be risky, because a new product or approach that is lucrative in times of crisis may not be sustainable. During the crisis, however, it can yield high returns. Roughly 9% of survey participants adopted this approach to deal with the pandemic.

Other firms must take steps that undermine the long-term well-being of the company. These retreating strategies assume that the firm will be damaged and either involve doing nothing or taking emergency steps that will harm the company in the long run. For instance, a farmer in a crisis might sell a cow that was producing milk that paid for school fees for his/her children, who could have earned a good income in the future as a result.

Many Filipino businesses laid off staff, sold assets or took on new debt to cope with COVID-19 – all of which may hurt their long-term viability. About 37% of the interviewees adopted one of these strategies and they, along with the 18% who did nothing, made up the 55% following this retreat approach.

Some types of companies were more likely to handle the crisis well. Firms that invested more resources in R&D before the pandemic tended to be more resilient or agile rather than adopting a retreating response to the crisis. These innovative companies did better during the pandemic: COVID-19 strongly affected 60% of firms that said they invested a high level of resources in research and development in 2019, compared to 83% of companies that dedicated low or no resources to R&D. This suggests they were both familiar with and able to take strategic initiatives for the long-term welfare of the enterprise.

Smaller firms reported weaker matching between the skills of their workers and their own needs. They also invested less in R&D and innovated less frequently. These traits meant they were less able to adapt and, as a result, less able to cope effectively when COVID-19 hit. A higher proportion of micro and small firms adopted a retreating approach, which could cripple their competitiveness in the future.

ITC's SME Competitiveness Grid (Chapter 1) features a pillar called 'capacity to change', which assesses the capacity of a firm to change in response to, or anticipation of, dynamic market forces. Firm scores for this pillar are calculated using SMECS responses to questions about finance, skills and innovation.

Econometric analysis reveals that a firm's capacity to change had a strong bearing on how it responded to the pandemic. Companies with a higher capacity to change were more likely to opt for resilient or agile responses to the pandemic.

The link between skills, R&D, innovation and resilience holds in most cases – but not all.

A higher proportion of women-led firms (49%) adopted resilient and agile responses than men-led firms (43%) – even though they have fewer resources available for research and they often struggle to find skilled workers and create new products. This suggests that women-led companies may be inherently resilient to business shocks. Investing in their business and integrating them more with the rest of the economy could make it easier for the Philippines to cope with future crises.

Similarly, a higher share of youth-led companies adopted resilient and agile strategies than firms led by their elder peers, despite their weaker mobilization of resources for change. Finally, while Calabarzon seems to excel at innovating in good times, its firms mounted a worse-than-average response to the COVID-19 crisis, with 69% of them retreating.

Filipino exporters and importers were much more likely to take a resilient approach than firms that did not participate in international trade. More than half (53%) of exporters and importers were resilient, compared to 36% of all interviewees. One reason for this is that trade teaches enterprises how to innovate, contend with challenges and access finance. That is, participation in trade strengthens the adaptive capacity of firms.

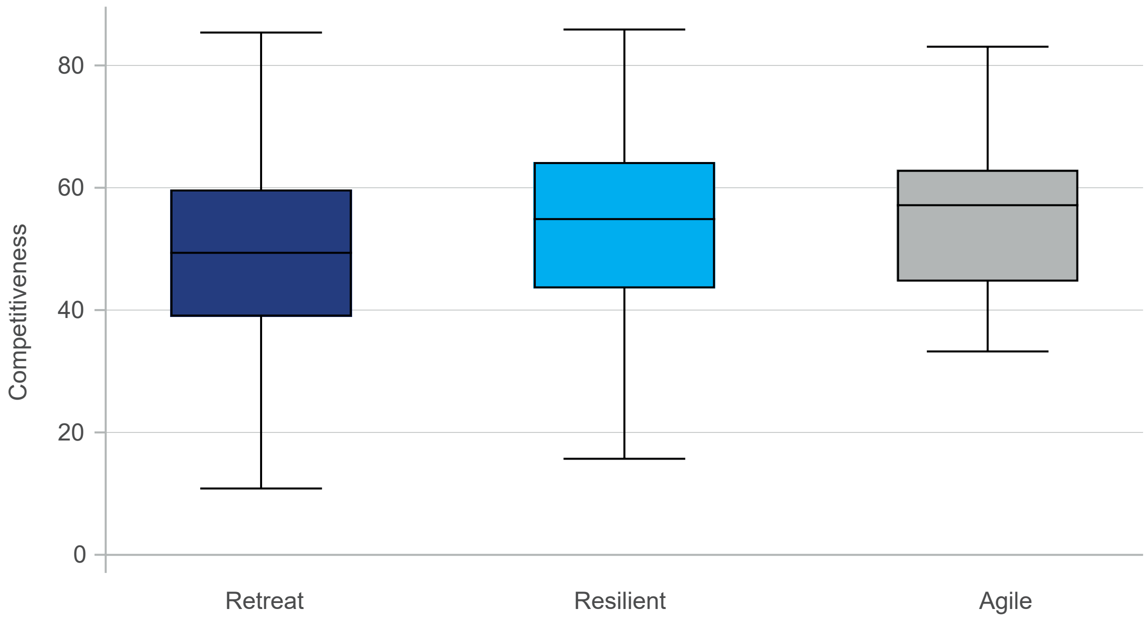
The capacity to change using skills, finance and innovation also has positive long-term implications for competitiveness, as noted earlier in this chapter. This means skills and innovation are key elements of resilience, as competitive companies are better at coping.

Evidence from both surveys shows that businesses that were more competitive before COVID-19 hit were more likely to adopt a positive, resilient response. Firms adopting a resilient or agile strategy had a higher median competitiveness score (Figure 14).

The figure shows that companies that were more competitive (with a higher score on the vertical axis) tended to adopt resilient and agile strategies (in the two boxes labelled 'resilient' and 'agile' on the horizontal axis). Companies that adopted either of these strategies had a higher median competitiveness score, shown by the higher horizontal line in those right-most boxes.

The fact that innovation and skills underpin resilient and agile strategies is important, because these approaches have been critical for enterprises to survive the crisis. Companies that adopted positive coping strategies were more likely to say they would survive the pandemic, survey data shows. In this context, it is significant that firms with a better capacity to change tended to adopt positive coping strategies.

Figure 14 Resilient and agile firms are more competitive



Note: The vertical axis measures the firm competitiveness score based on analysis of survey data. The middle line in the box above the word 'retreat' shows the median competitiveness score of firms that chose a 'retreat' strategy (as defined in the previous figure note). The bottom and top of the three boxes show the 25th and 75th percentiles respectively, while the 'whiskers' attached to the boxes show the extreme values of firms that chose that type of strategy. The box plots for 'resilient' and 'agile' are constructed similarly.

Source: ITC calculation based on SME Competitiveness Survey and ITC COVID-19 Business Impact Survey data collected in the Philippines.

Policy insight: Creating resilient small businesses

Efforts to shore up SMEs during the pandemic teach an important lesson: business resilience in good times is essential, as it can help companies ride out crises, reduce the likelihood of bankruptcy and improve the state of the economy.

The survey evidence suggests that companies with a stronger capacity to change and companies that import or export were more resilient to COVID-19.

Governments can promote SME adaptability through policies and programmes for skills, research and innovation. The fact that businesses headed by women or youth have a hard time finding workers with the skills they need suggests that the Philippines should take its education and training programmes to the next level.

The country could learn from successful initiatives, such as the *A Ganar Vencedoras* programme, which found that customized training programmes for young Brazilian women kept them engaged in the programme.[29] In the Philippines, customized training programmes could be created, or core training modules adapted, to include youth and women.

Incentives for investment in research and development, as well as innovation, can help firms become more resilient to crisis and to compete in dynamic, lucrative market segments. Importing and exporting also enhances the capacity to change and cope, so governments should continue to facilitate international trade.

Policies and programmes designed to make businesses more resilient to shocks can help boost their competitiveness while strengthening the economy as a whole. Public policy can support the resilience of small businesses – for example, by subsidizing investments in risk-mitigating technologies and fostering economic and trade diversification. Policies can also encourage partnerships, cooperatives and research that promote the development of agile new strategies.[30]

Finally, the resilience of SMEs also depends on the resilience of their ecosystems, including national governance institutions, business support institutions and infrastructure. Building the core governance quality of state and business ecosystems can bolster the stability and responsiveness of the institutions that help small businesses through hard times.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Chapter 4

Strong connections aid information flow

Strong connections aid information flow

Connecting to other business actors to get information and knowledge is crucial to competitiveness. Businesses that can build close ties with buyers, suppliers and institutions learn about new markets and how to access them. This is why a firm's capacity to connect – through telecommunications, contracts and membership in business associations, for instance – is essential.

Competitive forces are constantly changing in modern, open economies. Consumer trends, compliance requirements, environmental and health crises and trade flows are shifting rapidly and, in the process, are remaking the opportunities and risks for small businesses. The dynamic nature of today's markets implies that it is not enough for an SME to meet the quantity, cost and quality requirements of markets. To succeed, they also must connect with their business ecosystem to stay abreast of market dynamics.

On the one hand, being connected involves being informed about the nature of changes in the competitive environment. When a firm can 'connect' in this sense it gathers information about customers, suppliers, competitors, products, technologies and government policies.

On the other hand, connectivity also involves actively reaching out to provide information about the firm and its products. This means identifying potential clients and marketing goods and services to current and potential customers. In addition, it requires outreach to other actors in the business ecosystem, including those in the same value chain, cluster or sector.

Connecting with buyers fuels competitiveness

More than 60% of small businesses in the Philippines are connected to their buyers, according to the SME Competitiveness Survey (Figure 15). Some of these enterprises are collecting information about market requirements by producing to buyer specifications. Others export and gather market information from their counterparts overseas.

Foreign companies or multinationals partly or fully own a small share of Filipino firms, and they buy their output and instruct them on production methods. Of the 514 firms surveyed, 64% are connected to buyers through ownership, management or production specifications.

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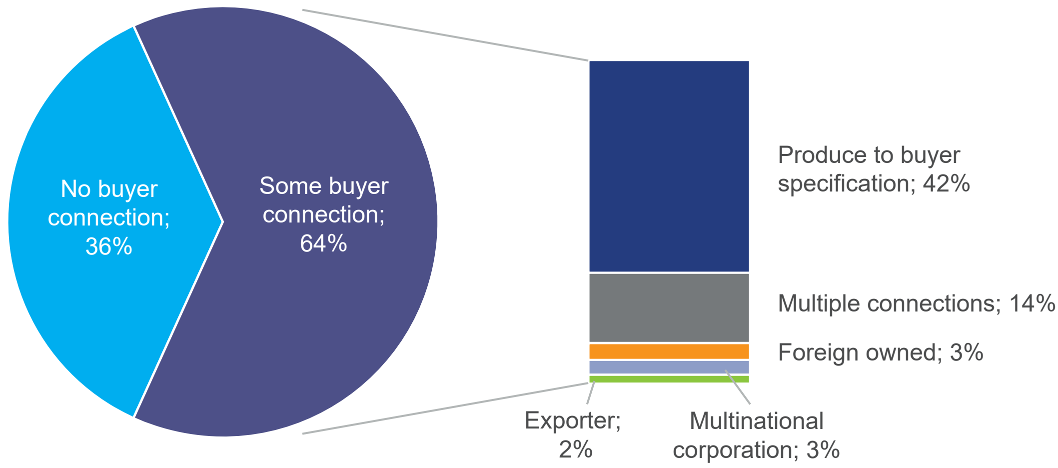
Figure 15 Three-fifths of firms are tied to their buyers



Note: Respondents were asked: 'Do you have a contractual relationship with your buyer, where you have to adhere to standards? (e.g. follow certain private/public standards or design specifications)?' Options included yes (partially), yes (fully), no and don't know. If they answered yes (partially) or yes (fully), they are included in the category 'produce to buyer specification' above. Respondents were included in the exporter category of buyer-connected firms if they gave a positive response to the question 'In the last full calendar year, what percentage of this establishment's sales were direct exports (e.g. products or services exported by this establishment?' Finally, firms are considered foreign owned if they indicated they were minority, majority or fully foreign-owned, or a multinational corporation or subsidiary.

Source: ITC calculation based on SME Competitiveness data collected in the Philippines.

Firms with any of these buyer connections appear to have more of the ingredients for competitiveness. They are far more likely to be able to prepare a business plan, for example. Buyer-connected firms in the Philippines also innovate more often than those that are not connected, according to analysis of the survey data. Finally, connected companies deliver a higher proportion of output on time than other firms.

This implies that the Filipino business landscape may have some characteristics of a dual economy: there is a subset of firms that are connected to buyers, and they become more competitive over time thanks to the information they glean from these networks. Other companies, on the other hand, appear to connect less and perform less strongly.

The tendency to connect varies widely by firm size and sector. Connecting was far more common in the manufacturing and service sectors than in the agricultural sector. In addition, larger companies were more likely to connect to their buyers than smaller enterprises.

Other research confirms that SME connections to other firms can be a valuable way to transfer knowledge. Small companies that supply to global value chains are exposed to modern technologies and business practices that can help them upgrade towards international standards of quality and competitiveness.[31] Indeed, the Department of Trade and Industry 7Ms for MSME Development framework highlights how models for large enterprise–MSME synergy can help small business owners be smarter entrepreneurs.[32]

Evidence to this effect comes from the Asian Institute of Management in a report showing that for SMEs, the main benefit of formal partnership and alliances (e.g. outsourcing, subcontracting, licensing and joint venture arrangements) with large firms was the knowledge transfer.

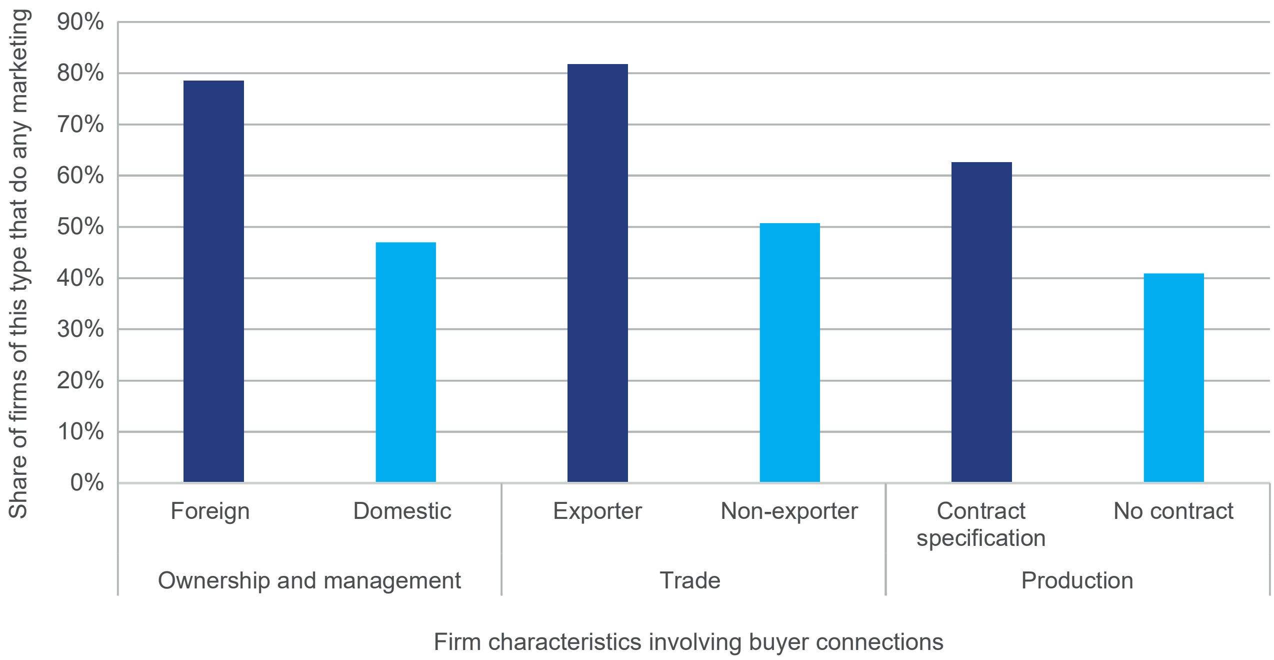
That study, based on data collected in Metro Manila, showed that small and medium-sized businesses have limited forward and backward linkages to large businesses. Just 7% of SME output was sold to a large company, and only 44% of domestically sourced inputs came from large firms.[33]

Need to improve outreach to new markets

Marketing activities help firms maintain and expand their market share, yet survey responses suggest that just half of Filipino SMEs advertise. Taken alongside the fact that only a third of these firms have a business website, the evidence shows that there is an opportunity to improve SME outreach.

When Filipino companies do advertise, they are most likely to use Facebook, other social media outlets, the internet or their own website to promote their offerings. This is not surprising, as Filipinos spend on average four hours on social media

Figure 16 Firms that connect to buyers tend to advertise



Note: The survey asked: 'In the last year, did this company engage in any of the following forms of advertising?' Response options are described in the previous question. The percentages in the figure measure the share of that type of firm that did any advertising. The definition of the type of firm is described in the notes to the previous figure.

Source: ITC calculation based on SME competitiveness data collected in the Philippines.

every day – the highest rate in the world – and nine hours a day on the internet.[34] Other forms of advertising, including print, radio and television, are less popular.

Advertising enables companies to find new buyers so they can diversify their revenue base and grow over time. Yet the tendency to advertise differs among firms. Evidence from the SMECS indicates that companies that are foreign managed or owned, or produce to specification, are considerably more likely to advertise to find new buyers (Figure 16).

Just 41% of companies that produce without a contract, and instead sell using spot or wholesale markets, advertise, compared to 63% of those that produce according to contract specification. Similarly, firms that export tend to advertise more than their non-exporting peers. And businesses that are partly or fully owned or managed by foreign actors are more likely to advertise than domestically run ones.

This evidence suggests that there is a virtuous spiral: entrepreneurs who connect with their buyers learn about their market and advertise to it, which in turn attracts more customers. This enables these entrepreneurs to thrive, grow and better connect with buyers. Indeed, there is a strong positive correlation between access to information about buyers and advertising in the Filipino data.

Other data from the Philippines confirms the synergies between connecting to current buyers and attracting new ones. Interviews with company owners in Metro Manila showed that partnering with large firms helped in outreach to potential clients.[35]

The policy implication of the foregoing analysis is that connecting to buyers is essential to upgrade the competitiveness of Filipino SMEs. Three-fifths of companies are already leveraging their connections for market performance and growth. Facilitating buyer connections for the other 36% of firms would spur advertising and competitiveness.

Broadening access to information and benefits

Firms that engage with business support organizations (BSOs) hope to access high-quality, current business information for management decision-making. As policymakers weigh how to improve their outreach to small firms – including to ensure that they obtain the information and benefits they need to survive future crises – they should consider broadening access to business support organizations.

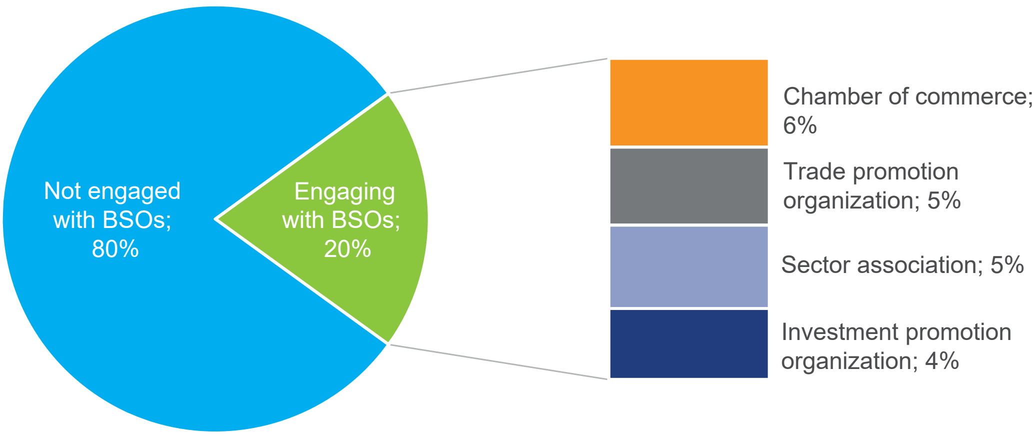
BSOs include:

- Trade promotion organizations (e.g. the Export Marketing Bureau or Center for International Trade Expositions and Missions);
- Investment promotion organizations (e.g. Board of Investments or Philippine Economic Zone Authority);
- Chambers of commerce (e.g. Philippine Chamber of Commerce and Industry);
- Sector associations (e.g. Philippine food processors and exporters organization or Philippine Exporters Confederation Inc.).

The data gathered for the SME Competitiveness Survey in the Philippines indicates that only a quarter of companies are involved with business support organizations (Figure 17). Roughly equal shares of interviewees engaged with each of the four types of support institution. These BSOs are part of a diverse network of institutions that have developed to support Filipino SMEs (Box 1).[36]

Figure 17 Just 20% of firms engage with support institutions

Percentage of firms engaging with business support organizations



Note: Respondents were asked: 'Are you actively engaged with any of the following types of institutions?' They chose 'yes' or 'no' for each of the following: trade promotion organizations (e.g. EMB or CITEM), investment promotion organizations (e.g. BOI or PEZA), chambers of commerce (e.g. PCCI), and/or sector associations (e.g. PHILFOODEX or PHILEXPORT).

Source: ITC analysis based on SME competitiveness data collected in the Philippines.

The tendency to connect to institutions varies by the region where the business is based. Engagement was most common in Calabarzon, where 26% of interviewees said they have engaged the services of a BSO. It was slightly less popular in Cebu City (22%) and the National Capital Region (20%), while just 13% of surveyed firms in Central Luzon had institutional connections. Furthermore, firms that are large, led by men and in the service sector are more likely to engage with business support organizations.

The fact that institutional connections are more common in Calabarzon is worthy of further attention, especially as the region is strongest when it comes to meeting quality requirements. The survey data indicate that firms in Calabarzon are also more likely than enterprises in other regions to exchange information among themselves and to deliver goods and services on time.

Calabarzon's business ecosystem seems to be different from elsewhere in the country, and for the better. The region scores substantially higher on virtually all business ecosystem measures in the competitiveness survey. While it is difficult to attribute this strong performance to a specific factor, contributing factors include the dynamism of the region's industrial estates, the strong infrastructure including at the Port of Batangas, and high rates of investment.[37]

Across the four surveyed regions, involvement with business support organizations helped companies connect to business information. Firms that said they engaged with a BSO gave much higher ratings to the availability and quality of market information on potential suppliers than companies that did not engage with a BSO. Connecting to information on suppliers can improve the quality and predictability of inputs, which helps firms meet market quality requirements.

In addition, firms that were involved with BSOs exchanged much more information with other companies in their sector. Connecting with other firms in the sector can support the development and sharing of product and service innovations. This, in turn, improves the capacity to compete on quantity and cost grounds. Evidence from the Philippines indicates that BSOs regularly contribute to both phenomena.

What's more, firms that are better connected tend to have habits that improve their competitiveness. The 88 firms that are involved with BSOs and share information with companies in their sector were more likely to export, innovate, have a business plan and produce to the specifications of their buyers.

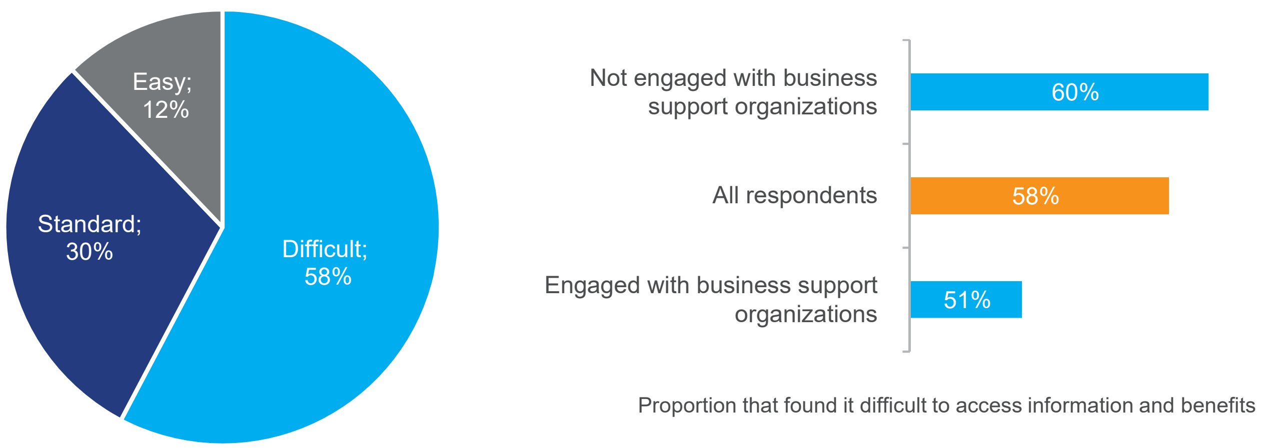
This shows that Filipino firms that connect with BSOs and leverage those connections for sector-wide networking have a winning strategy that enables them to become internationally competitive. In this context, the fact that just one in four businesses is involved with a BSO indicates that further efforts are needed to reach out to additional SMEs.

Connecting helped firms keep current about COVID-19

Companies with strong connections to their buyers, suppliers and business support organizations had a ready support network when the pandemic hit. Indeed, the evidence suggests that these firms were better able to communicate and marshal the information and support they needed from their business ecosystem to better adapt and survive the crisis.

The COVID-19 crisis has underscored the importance of access to information in the days and weeks following a shock. Businesses need the details of the market situation and to find out what support is available to them. Yet more than half of all companies (58%) found it difficult to find out about COVID-19 government programmes (Figure 18).

Figure 18 Firms struggle to access COVID-19 information and benefits



Note: Respondents were asked: 'How easy is it to access information and benefits from government COVID-related SME assistance programmes' and 'Are you actively engaged with any of the following types of institutions: trade promotion organizations, investment promotion organizations, chambers of commerce or sector associations?' Companies are considered to be engaged with a business support organization if they said they were involved with any of the four types of institutions. Interviewees who chose 'very easy' or 'easy' on the COVID-19 information question are classified as 'easy', while those who chose 'very difficult' or 'difficult' are classified as difficult'. Those who chose 'standard' are shown as 'standard'.

Source: ITC calculation based on ITC COVID-19 Business Impact Survey data collected in the Philippines.

Firms that already had connections to their business ecosystem found it easier to access virus-related government information and benefits. Being engaged with a business support organization reduced the likelihood of finding it

difficult to get information and benefits by 9 percentage points, from 60% to 51%.

Companies that were partly or wholly foreign owned were also less likely to find it difficult to get help when the crisis struck. Just 49% reported difficulties, compared to 58% in the full sample. Finally, a notably higher share of enterprises that exported their wares overseas said it was easy to obtain information and benefits from government COVID-19-related assistance programmes.

In the case of real socioeconomic disaster, one can do little to prepare, and the market will not offer the support that businesses need to survive catastrophic situations. In such situations, government can step up and provide a public good in the form of support to sustain SMEs through the crisis.

The Filipino government has put in place several measures to help SMEs survive the pandemic. Commercial rent due during the containment period was officially deferred for a month without any interest penalties, fees or other charges. Borrowers from the Small Business Corporation were granted a one-month loan moratorium.

On the financing side, a 1 billion Philippine peso ($20.3 million) Enterprise Rehabilitation Financing facility was created for loans to micro and small enterprises with at least one year continuous operation before March 2020, and whose sales fell drastically.

The Department of Trade and Industry launched the Livelihood Seeding Programme through local Negosyo centres to support affected businesses. This includes financial support packages ranging from 5,000–8,000 pesos ($100-$160) that are expected to reach 18,000 SMEs. The trade department also organized free webinars during the ECQ to show SMEs how to take their businesses online.

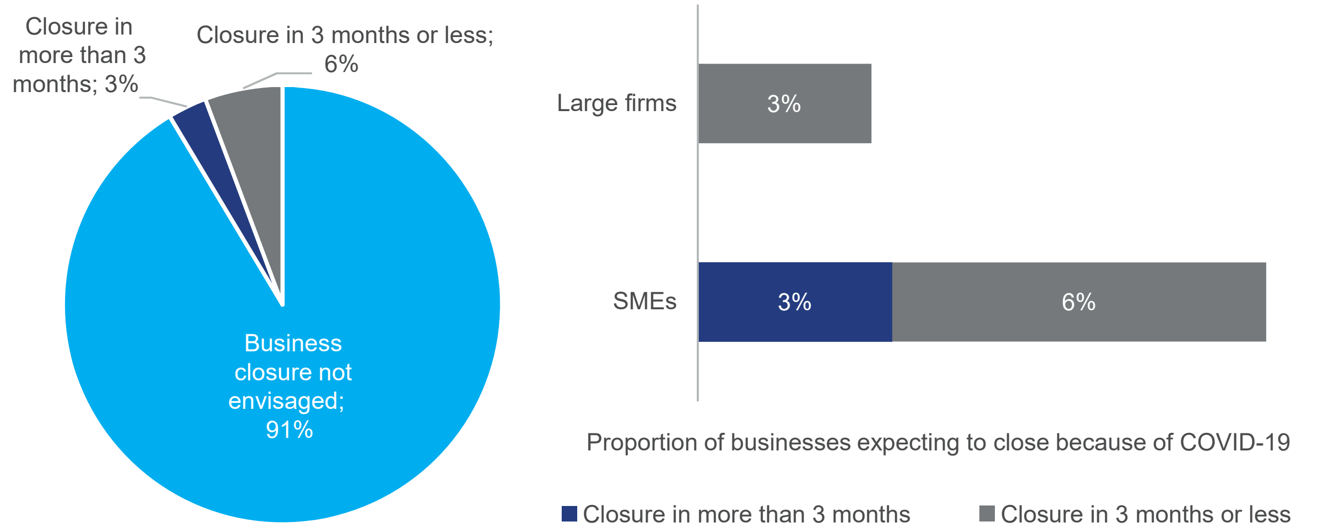
The government gave an unconditional cash transfer of 5,000 pesos ($100) to rice farmers in 42 provinces not covered by other programmes and/or especially affected by the drop in rice prices.[38] Finally, the COVID-19 Adjustment Measures Program granted cash transfers to formal sector workers and the *Tulong Panghanapbuhay sa Ating* Disadvantaged/Displaced Workers programme provided emergency employment assistance to informal sector workers.

Economic crises often lead to the bankruptcy of businesses that would otherwise be viable and add value to the economy. The market generally fails to prevent this outcome. The COVID-19 pandemic is no exception: 9% of all survey respondents expected to close permanently as a result of the crisis.

Connections to the business ecosystem – and thus access to information and benefits – had a real impact on the experiences of Filipino firms with the pandemic. Ten percent of firms that said it was difficult to access information and benefits predicted their own collapse because of the crisis, compared to 6% of firms that said such access was ‘standard’ or ‘easy’.

The above analysis shows that measures taken to contain the spread of COVID-19 have had a bigger impact on SMEs, which are less likely to adopt resilient strategies to cope. In this context, it is not surprising that small companies were twice as likely as larger firms to report that they expected to shut down permanently within three months (Figure 19).

Figure 19 Nine percent of SMEs expect to shut down



Note: Respondents were asked 'Do you think there is a risk that your business will permanently shut down because of this crisis, and if so, when could this closure occur?' and 'How many full-time employees does the business have?'

Source: ITC calculation based on ITC COVID-19 Business Impact Survey data collected in the Philippines.

In this dataset, the higher exposure of trading firms to disruption seems to have outweighed their greater resilience. Companies that exported and imported were more likely than others to say they expected to shut down permanently in the future because of COVID-19. Youth-led firms and those based in Cebu were also more likely to expect to fold.

Although the fact that almost one in 10 firms expects to shut down is sobering, this rate is lower than elsewhere in the world. Enterprises in 126 other countries answered the same question in the ITC COVID-19 Business Impact Survey, and the percentage predicting closure was much higher. For example, 36% of interviewees in other Asian countries said they were at risk of shutting down.

Policy insight: Nurturing connections for business information

There are opportunities to strengthen the connections between small Filipino firms, suppliers, buyers and business support organizations. Survey findings show that better linkages would enhance both SME competitiveness and their ability to mobilize help in times of crisis.

Well before the pandemic hit, public sector institutions such as the Negosyo centres provided support that boosted SME competitiveness and improved their capacity to deal with the COVID-19 shock. Yet a high proportion of Filipino enterprises are not connected to any business support organization. Reaching out to small firms in subsectors with high export potential and encouraging them to engage with BSOs could improve their competitiveness, trade flows and resilience.

ITC's 15-point action plan highlights how business support organizations have played a central role during the crisis to channel the flow of trusted information from a business perspective, for example, through a specialized webpage.

In addition, good business support organizations benefit from their knowledge of business, their convening power and their credibility to represent SMEs, make their needs known among policymakers and funders, and build bridges to deploy solutions rapidly.

These institutions also have a crucial role in supporting business recovery for inclusion. They should take the opportunity provided by COVID-19 response to shift some of their support away from existing businesses to innovative start-ups, from urban to rural areas, and towards climate-friendly and socially responsible sectors.[39]

Chapter 5

Policies for resilience and competitiveness

Policies for resilience and competitiveness

Small and medium-sized enterprises are at the vanguard of the Philippines' emergence as a global economic powerhouse. As the country comes into its own in regional and global trade flows, it depends upon the small businesses that supply into its value chains and sustain its economy.

Thriving SMEs support not only the economy at large – they are crucial sources of livelihood for the millions of people who work for them. This is why their competitiveness and resilience is of deep interest to policymakers across the country.

This report finds that while many Filipino businesses are globally competitive and have been able to weather the pandemic, others are fighting to survive.

There is a real gulf between thriving SMEs, which are exporting, innovating and getting certified, and the many others that are not connecting with their buyers and are stuck in low-margin markets with weak cash flow. The measures taken in early 2020 to stem the spread of the pandemic have taken a heavy toll on many of these small businesses, which are seeking help as they try to avoid bankruptcy.

Greater competitiveness is key to resilience

This report describes the characteristics of firms that coped better with the COVID-19 crisis. Companies that were more competitive tended to be more resilient, surviving the pandemic with their basic form intact. As such, the first step in preparing Filipino SMEs for the next crisis – and ensuring they recover from the pandemic – is to address key constraints to their competitiveness.

Address management and cash flow constraints

Analysis of the survey data shows that a large number of companies in the Philippines can compete in the short term. However, many are grappling with poor inventory management, low capacity utilization and poor cash flow management. Indeed, the firm-level data reveals serious cash flow constraints in many enterprises.

Access to short-term financing is another major constraint. Combined with widespread problems with delayed payments and very tight competition, many companies face short-term difficulties, without the capital or security to plan or invest in the long term.

A careful look at government public procurement plans, and specifically their provisions for timely payment and reservations to SMEs, could help address this issue. Improving the judicial remedies for unpaid contracts could also prove worthwhile.

Extend access to the right skills to all firms

While Filipino SMEs excel at mobilizing the skills and innovation needed for today's knowledge economy, some types of firms have been left out. Customizing skills training to ensure that youth- and women-led companies can access suitable workers will help them build their capacity to change.

Skills, research and innovation are essential to the future competitiveness and resilience of small firms. Interestingly, enterprises that invest in research are more resilient and agile – as are those led by women and youth. Participation in international trade also encouraged resilience.

Attention to the factors driving these positive coping strategies is essential, as they reduce the chances of business closure during a crisis.

Weak ties to business ecosystem cripple competitiveness

Small enterprises in the Philippines excel at changing according to market demands using strong skills and innovation capabilities. However, they have relatively weak connections with the buyers, suppliers and business support

organizations in their business ecosystem. A very high proportion of Filipino firms are not connected to any support institution.

This makes it difficult for SMEs to gather the information they need to become more competitive. As a result, many have struggled to withstand the difficult conditions during the ECQ.

Report findings show the value of better linkages between small businesses, their buyers and business support organizations. Reaching out to these firms, particularly those in subsectors with high export potential, and encouraging them to engage with BSOs could help boost their competitiveness and trade flows, as well as resilience.

Building a robust business ecosystem

The experience of the COVID-19 crisis has shown that small firms operate in a business ecosystem that influences whether they will sink or swim in the 'new normal'. They depend on the policies, programmes and governance of the institutions in the business ecosystem around them. Although connections to business support organizations are important, the links that connect these enterprises with other supply chain actors must also become more resilient.

All supply chain actors have a role to play in building more inclusive and resilient supply chains – from the governments that regulate them to the consumers choosing which brand to buy. However, lead firms often have an important role in directing supply chains, making decisions about production practices, branding, sourcing and sales.[40]

In many cases, lead firms have passed the risk burden along the supply chain to vulnerable small businesses in developing countries.[41] As a result, disruptions lead to job losses and bankruptcies, as well as insufficient supply to the lead firm and its customers.

Better contracts between value chain buyers and SME suppliers can facilitate the sharing of risk. Indeed, when buyers provide risk insurance services through contracts, it can attract suppliers and encourage them to invest in producing higher-quality output to foster long-term, stable buyer-supplier relationships.[42]

Helping small firms prepare for the new normal

Four long-term trends will characterize the new normal on the horizon: an emphasis on resilience to shocks, embracing digital opportunities, greater inclusiveness and sustainability. Policymakers can help small and medium-sized enterprises participate in building this new reality – or at least, not being left behind by it.

Resilience

Policies and programmes that target the resilience of businesses to shocks can help boost their competitiveness while helping the economy as a whole withstand the next storm. This can include encouraging participation in international trade and innovation.

Public policy can also play a direct role in building the resilience of small businesses – for example, by subsidizing investments in risk-mitigating technologies and fostering economic and trade diversification. Policies can also encourage partnerships, cooperatives and research that promote the development of agile new strategies.

Finally, the resilience of SMEs also depends on the resilience of their ecosystems, including national governance institutions and business support institutions and infrastructure. Building the core governance quality of state and business ecosystems can bolster the stability and responsiveness of the institutions that help small businesses through hard times.

Digital

Digital technologies were already ascendant before the pandemic. Businesses operating online were able to avoid the full effect of the crisis as consumers shifted to online shopping. Government policy can learn from this success and facilitate small business use of digital technologies to reduce their exposure to future crises. Investments in expanded e-payment infrastructure, for instance, can help reduce exposure to shocks to the cash economy and build the competitiveness of remote enterprises.

The use of digital trade facilitation processes can also ensure that trade continues despite disruption. Clearance procedures based on electronic documents and payments are simpler, faster and safer, limiting in-person interactions between traders and border authorities. In addition to digital processing of paper-based documents, governments can consider issuing original documents electronically.

Inclusive

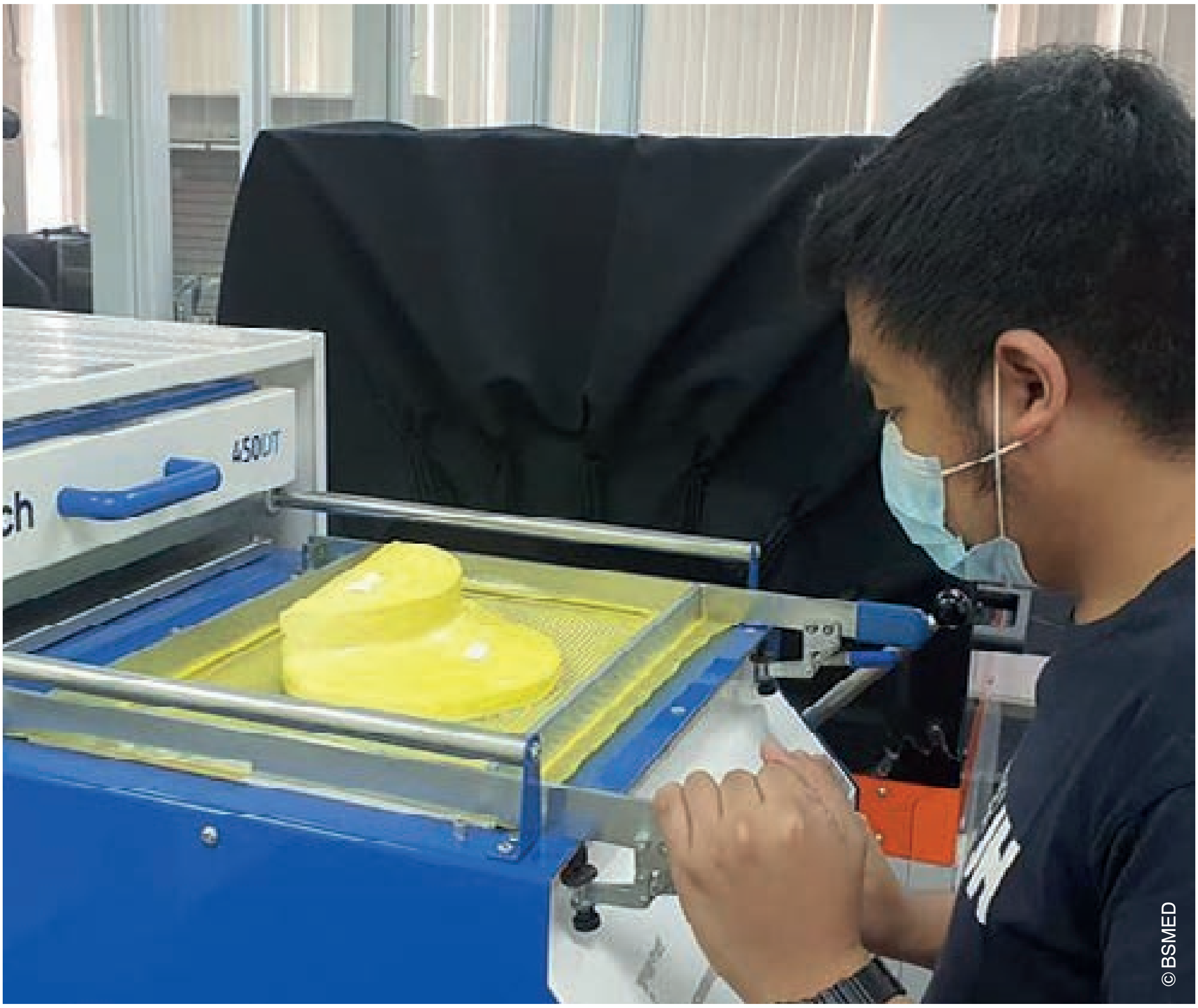
More inclusive and resilient supply chains are needed to protect small businesses, and their customers, from the next crisis. Lead firms should redesign their approach to collaboration and costing with SME suppliers to ensure more equally shared value. The mutual trust that results encourages sharing of information and collective action to overcome challenges.

This ‘social capital’ in the supply chain can be crucial to transmitting information and funds as necessary and to responding to crises. The way the supply chain is managed and developed over time can foster an agile work culture that improves the capacity to adapt.

Sustainable

The COVID-19 recovery effort provides an opportunity to ‘build back better’, investing in sustainable production processes. Environmental concerns remain high on the agenda, especially given evidence that the next crisis will come from this front.

To reduce the severity of future climate change, and help small Filipino firms contend with its effects, attention must focus on green growth opportunities. Sustainability is likely to be more important in the post-pandemic global economy, and retrofitting for both COVID-19 sanitary requirements and environmental friendliness may be wise.[43]



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Appendix

About the SME competitiveness survey

About the SME competitiveness survey

ITC analyses competitiveness using the three competitiveness pillars and three levels of the SME Competitiveness Grid (Figure 1). Each pillar is further subdivided into three themes. Although it was designed to focus on the competitiveness of small and medium-sized enterprises, the framework can also be used to assess the competitiveness of bigger firms.[44]

The SME Competitiveness Grid

The three pillars of competitiveness are compete, connect and change.

- **Capacity to compete**: The first pillar refers to the static dimension of competitiveness, focusing on the current operations of firms and their efficiency in terms of cost, time, quality and quantity themes. This concept also extends to the immediate business and national environment. Examples of determinants include use of internationally recognized quality certificates (firm capability); access to technical infrastructure (immediate business environment); and low tariffs (macro-environment).

- **Capacity to connect**: The second pillar centres on gathering and exploiting information and knowledge. At the firm level, this refers to efforts to gather information flowing into the firm (e.g. consumer profiles, preferences, and demand), and efforts to facilitate information flows from the firm (e.g. marketing and advertising). At the immediate business environment level, this includes links to sector associations, chambers of commerce and other business support organizations. At the national level, the capacity to connect is predominantly about the availability of information and communications technology infrastructure.

  The capacity to connect is not strictly a time-sensitive phenomenon. However, gathering and exploiting information is so fundamental to current and future competitiveness that they act as an essential link between the two pillars of static competitiveness and dynamic competitiveness.

- **Capacity to change**: The third pillar targets the capacity of a firm to make changes in response to, or in anticipation of, dynamic market forces, and to innovate through investments in human, intellectual and financial capital. It incorporates the dynamic dimension of competitiveness. Industry phases and breakthrough or disruptive innovations all require strategy adaptations. Thus, the capacity to change incorporates how well firms access finance and invest in human capital, innovation, and intellectual property protection. At the business or macro-economic level, the environment's ability to deliver these resources to firms is measured.

These three pillars of competitiveness can be examined at three levels of the economy.

- At the **firm level**, their ability to manage resources adeptly influences their competitiveness.

- At the **business ecosystem** level, factors that support firm competitiveness but are external to the firm, including the availability of skilled workers, infrastructure and business support organizations, are important.

- The **national environment** includes the macroeconomic and governmental factors that establish the fundamentals for the functioning of markets in the economy.

The SME Competitiveness Grid bridges a gap in composite indicators that focus on macroeconomic determinants of competitiveness rather than local or microeconomic determinants. The importance of macroeconomic determinants is, however, fully recognized and reflected in the 'national environment' level of the grid. ITC's SME Competitiveness Outlook 2015 provides a more detailed description of the SME Competitiveness Grid and the methodology behind it.

What are SMEs?

This report defines small and medium-sized enterprises as companies with fewer than 100 employees. The term 'SME' thus includes micro-sized firms, understood as those with fewer than five employees. It also covers small companies with 5–19 employees and medium-sized ones with 20–99 employees.

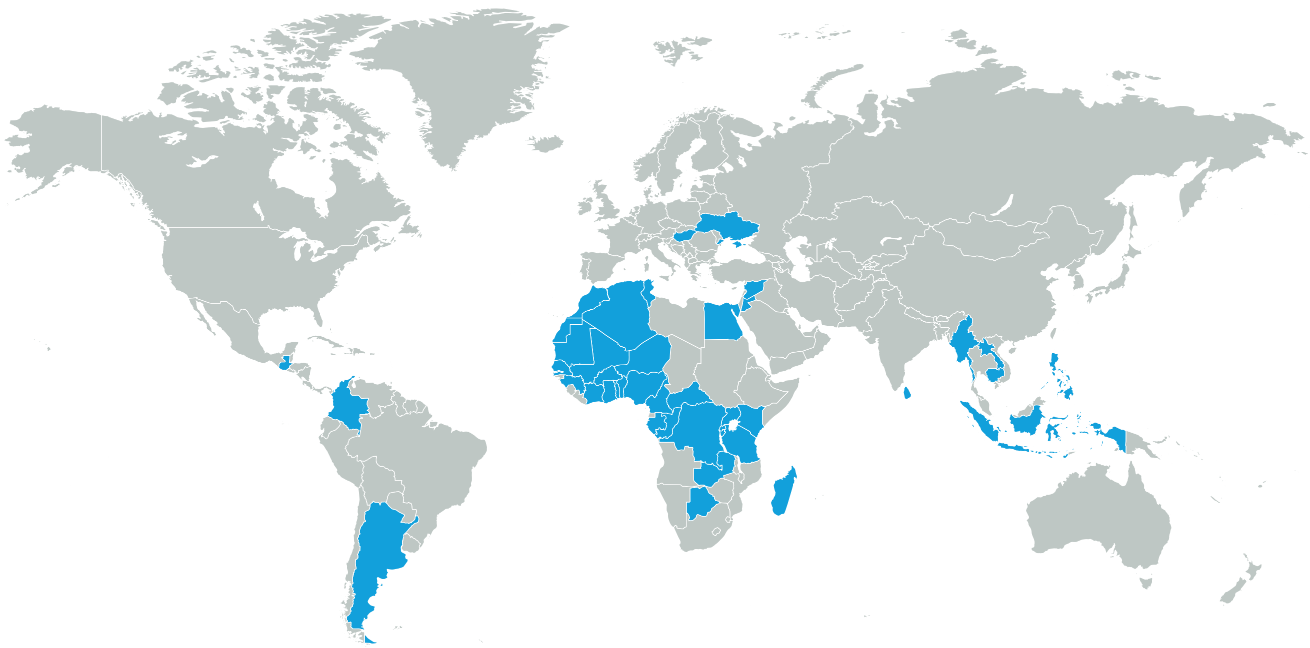
This definition is different from the legal definition of an SME in the Philippines, which is based on asset size. The National Statistics Office of the Philippines uses yet another definition that is based on number of employees. The table below clarifies and compares these definitions.

	This report	Legal definition in the Philippines[45]		Statistical definition in the Philippines
		Asset size in Philippine peso	Asset size in US dollars	
Micro	Four or fewer employees	P3,000,000 or less	$60,000 or less	Nine or fewer employees
Small	Between five and 19 employees	Between P3,000,001 and P15,000,000	Between $60,001 and $300,000	Between 10 and 99 employees
Medium	Between 20 and 99 employees	Between P15,000,001 and P100,000,000	Between $300,000 and $2,000,000	Between 100 and 199 employees
Large	100 or more employees	More than P100,000,000	More than $2,000,000	200 or more employees

How to measure SME competitiveness?

Measuring all dimensions of competitiveness can be difficult. ITC created the SME Competitiveness Survey (SMECS) to allow countries to collect the data they need to measure the competitiveness of their enterprises. As of August 2020, almost 18,000 companies in 46 countries, including the Philippines, had been surveyed (Figure 20).

Figure 20 SME competitiveness surveys across the world



Source: ITC

The SMECS is typically deployed in partnership with domestic business support organizations (BSOs). ITC gives these institutions the software to collect and maintain an active database on micro, small and medium-sized enterprises, and assists BSO staff with sample selection and training the team of interviewers.

The SME Competitiveness Survey helps governments and BSOs better understand the needs of their enterprises. The tool is designed to combine information at the macro (national business climate), meso (local support ecosystem for businesses) and micro (firm capacity) levels to provide a nuanced picture of the capacity of a country's private sector to compete in international markets.

Policymakers and BSOs can use the findings to identify and address bottlenecks to competitiveness; to compare the competitiveness of firms based on size, sectors and location; and to better match firms with potential investors and buyers.

How to understand SME competitiveness?

The report uses the conceptual framework described above to analyse the Philippines SME Competitiveness Survey data and assess the competitive position of small and medium-sized companies in the country. The report provides highlights of the analysis of that data, given the limited space available. More analysis was conducted, and indeed additional information can be further extracted from the data.

The report analyses data from three levels in the SME Competitiveness Grid: national, ecosystem and firm level. The national environment is examined based on a review of secondary data and related literature. Firm and ecosystem-level competitiveness is analysed from firm-level survey data collected through the SMECS.

A disaggregated analysis of the SMECS dataset in the Philippines yields additional insights on the competitiveness themes discussed in the report. Subsamples from each sector are analysed to assess sector-specific challenges and strengths. Results vary by firm size, defined according to number of employees. Micro firms are defined as those with four or fewer employees; small firms have 5–19 employees; medium-sized ones have 20–99 employees; and large firms have 100 or more employees.

Women-led and youth-led firms are compared to their peers. Women-led firms are managed by a woman and at least 30% owned by women, while youth-led firms are defined as being run by a top manager under age 35.

Where relevant, and notably in the conclusion, policy recommendations highlight opportunities to address issues identified in the analysis of the data.

Endnotes

1 SME reservations in public procurement rules reserve a certain percentage of procurement for SME suppliers.

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