



Task Force 1
Macroeconomics, Trade, and Livelihoods:
Policy Coherence and International
Coordination



THE MERITS OF AN INTERNATIONAL MSME ALLIANCE

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Vinod Kumar Wuthoo, President, India SME Forum


Maria Valeria Pasquini, General Co-ordinator, World Union of SMEs

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Abstract





According to the International Labour Organization (ILO), self-employment, and micro and small businesses provide more than two-thirds of the total employment in underdeveloped and developing countries, and play an important role in their economies.¹ If not for the massive obstacles that stifle and threaten their potential, micro, small, and medium enterprises (MSMEs) will add significant value to their countries' economies.


However, most governments have not fully realised the promise of MSMEs, given the lack of best practice-sharing on ecosystem development, policies, strategies, technical skills, and expertise that are essential for developing an MSME ecosystem, and the limited linkages to global value chains. It is imperative that G20 member countries come together to form an 'International MSME Alliance' to create a wider ecosystem for MSMEs worldwide.



The Challenge

1






Micro, small, and medium enterprises (MSMEs) have a significant impact on how growth, innovation, and sustainability are enabled and shaped in the national, regional, and local economies. MSMEs contribute to 90 percent of business, over 60 percent of employment, and 50 percent of national income (GDP) worldwide.² According to the World Bank, 600 million jobs will be required by 2030 to accommodate the world's labour force, making the growth of MSME a top priority for many governments.³

MSMEs employ roughly 89 percent of all workers in the private sector in the East Asia and Pacific region (11 economies), 69 percent in the Europe and Central Asia region (31 economies), 62 percent in the Latin America and Caribbean region (15 economies), 73 percent in the West Asia and North Africa region (8 economies), 53 percent in the North America region (three economies), 85 percent in the South Asia region (four economies), and 64 percent in the Sub-Saharan Africa region (five economies).⁴

However, MSMEs, especially those in underdeveloped and developing

countries, face substantive challenges related to finance and capital, lack of relevant skills, knowledge about international markets, non-tariff barriers, cumbersome regulations and border procedures, restricted access to trade financing, market entry, and competition policy issues. These challenges hinder the growth prospects of MSMEs and limit their longevity and potential for wider contributions.

- **Absence of a thriving ecosystem for MSMEs:** Large enterprise can thrive in a business-friendly environment and open markets, but due to their small size, many MSMEs find it challenging to obtain the necessary skills and resources, including people who possess the latest information on management techniques, finance, and technology, that would increase their productivity. In view of the challenges faced by MSMEs and the scale of the opportunity, most G20 countries have set up a national body that is completely or primarily in charge of assisting in their expansion. Nevertheless, operating these government entities is difficult due to the same factors that have made it difficult for markets to



meet the demands of MSMEs: their small size weak infrastructure, poor functioning of regulatory environment, limited access to resources, and lack of business skills and knowledge. Governments and other institutions everywhere are starting programmes to provide them with the advisory assistance they need to deal with the situation but that is not enough.

- **Constraints over market expansion:** According to a McKinsey report, several studies reveal that MSMEs need to internationalise to grow, but they often struggle to do so strategically or outside of their home market.⁵ High-potential MSMEs in many markets achieved domestic success even before the COVID-19 pandemic, but their potential was constrained by the size of their local market. Unlike large businesses, many MSMEs lack the capacity to carry out in-depth market research before entering new markets, opting instead to take advantage of opportunities and grow marginally.
- **Downward turn of GVCs:** Global value chains (GVCs) today make


up nearly 50 percent of the global trade.⁶ The emergence of GVCs and international trade have had a substantial impact on development over the past 30 years. Income and productivity have increased, especially in developing nations, as it creates job opportunities. For instance, the boom in exports to the US following the US-Vietnam Bilateral Trade Agreement in 2001 boosted the wages of unskilled workers, reduced the skill premium, and was a key driver of poverty reduction in Vietnam.⁷ Nevertheless, there are reasons to be concerned that this trade-driven path to development is in jeopardy. Nations need to cooperate on a variety of issues to improve the current system. Given that foreign investment regulations are inconsistent, and state-owned enterprises distort the market, agriculture and services need coordinated trade liberalisation. Developing nations must increase social assistance and labour norm compliance to increase job opportunities and income gains from participation in GVCs. The landscape of global trade and GVCs is currently undergoing substantial changes,

but uncertainties remain. These may be linked to factors like the geopolitical situation, technological advancements, and increased concerns about sustainable and inclusive development. However, it is still possible to revive commerce, growth, and GVCs. Progress depends on commerce, but for commerce to function effectively, there must be government-mediated regulations.

- **Complex policy and regulatory frameworks:** Technical rules, adherence to environment, health and safety standards, labour laws and regulations, and taxation and financial reporting present entry-level obstacles to MSMEs. Lack of transparency and overly cumbersome regulatory procedures may prevent the formalisation of unregistered MSMEs, hence reducing their ability to support local economic development. Coherent regulatory frameworks for MSMEs can help lower entry barriers, facilitate access to finance, encourage innovation, and promote competition, all of which can improve productivity, growth, and job creation in the MSME sector and

ultimately create an environment that is favourable for MSMEs to flourish.

- **Securing and managing funds:** MSMEs often have trouble obtaining financing from conventional sources like banks and financial institutions due to their bad credit histories, lack of collateral, and high-risk profiles. Effective money management is also essential for long-term success. MSMEs are unable to explore prospective growth possibilities, market advantages, and strategic movements because of a lack of funding or poor financial management. By implementing effective financial management practices and exploring alternative funding sources, MSMEs can enhance their ability to seize these opportunities and drive long-term success. As a result, it is critical for MSMEs to implement strong financial management techniques, such as making a realistic budget, monitoring cash flow, and seeking expert advice when necessary. Moreover, MSMEs can consider alternative funding sources including venture capital, crowdsourcing, and peer-to-peer lending platforms,



which can provide finance with less constraints than traditional lenders.

- **Technology a deterrent:** MSMEs can use technology to increase efficiency, competitiveness, and innovation. MSMEs may lack the necessary expertise to adopt and utilise the right technology for

their business needs because they struggle to keep up with the rapidly evolving technological landscape due to a lack of resources and knowledge. Furthermore, the cost of integrating new technology and upgrading old systems can be a significant hurdle for MSMEs.



The G20's Role



2



Currently, there are no international active inter-governmental alliances for MSMEs. This gap must be filled to ensure that MSMEs worldwide can be brought under monitored supervision, to resolve many of the issues plaguing the sector. As a premier forum for international economic


cooperation, the G20 is the most fitting platform to build the framework for an 'International MSME Alliance'. The G20 can pioneer the global MSME revolution because its membership includes industrialised and developing nations that together account for 85 percent of the global GDP.⁸



Recommendations to the G20



3



There are roughly 365-445 million MSMEs in emerging countries, of which 25-30 million are formal SMEs, 55-70 million are official microbusinesses, and 285-345 million are unregistered businesses.⁹ This highlights the need and urgency for a sophisticated global MSME network.


An International MSME Alliance can be a pivotal step in creating a platform for MSMEs worldwide to exchange best practices, technological know-how, and expertise to develop a world-class ecosystem. Such an alliance can empower MSMEs to achieve long-term efficiency and global competitiveness, allowing them to thrive in a highly competitive business environment. Utilising the collective knowledge and resources of MSMEs from around the world, the proposed alliance can promote growth, innovation, and entrepreneurship.

If formalised, the International MSME Alliance will encompass and address the entire spectrum of the MSME, recognising and transcending the significance of all categories and sectors, including retail, manufacturing, services, high-growth startups, and digital-only businesses. This inclusive

approach acknowledges the diverse nature of MSMEs and the vital role they play in the global economy. It effectively allows the alliance to honour the synergies and interdependencies among different segments, fostering collaboration, partnerships, and knowledge transfer that can drive innovation, productivity, and inclusive growth. The proposed alliance then seeks to create an inclusive and supportive ecosystem that nurtures the aspirations of MSMEs across various categories and sectors, ensuring their sustained growth and contribution to the global economy.

This alliance will consist of representation from developed, developing, least developed, and landlocked developing countries to comprehensively address the diverse needs and challenges of MSMEs across different global contexts. Collaboration between these nations can promote information exchange, capacity development, and policy coordination to the advantage of all concerned MSMEs.

The G20 can propose and support the formation of the alliance with a secretariat, preferably in India, and encourage participation from developed, developing, least developed, and




landlocked developing countries. It can aid the alliance with financial and technical assistance, encourage policy coordination, facilitate information exchange, and establish a constitution and monitoring procedures. These actions will foster greater collaboration, information exchange, and capacity development through policy coordination to the advantage of all MSMEs involved, promoting inclusive and sustainable economic growth globally.

Common indicators and mechanisms

Some countries have high manufacturing shares, low service shares, and high or satisfactory wholesale and retail shares. In other countries, the shares of the manufacturing, whole and retail sectors are lower when compared to their services sector, which may have a dominant economic hold. Certain effective parameters for MSMEs from the developed countries can be applied in the emerging economies, after modifications based on demographic and regional considerations. A common indicator and mechanism system can facilitate this and help countries increase their manufacturing, services, and wholesale-retail shares.

There are no prevalent common indicators that differentiate between micro, small, and medium enterprises. The US,¹⁰ Canada,¹¹ and some European economies¹² classify MSMEs based on the number of employees that work in a particular enterprise unit.¹³ India, however, categorises MSMEs based on their turnover and investment infrastructure. The International MSME Alliance can be used to build a standard nomenclature for a uniform category that is best suited for all economies. This would necessitate the creation of a uniform indicator that is widely acknowledged by all economies.

The International MSME Alliance can use these indicators to develop mechanisms that will guide future efforts to develop MSMEs in all countries. These mechanisms can help create a ranking system to evaluate MSMEs based on parameters such as financial capacity, market reach, growth and life cycle, and digital adoption. The ranking system can display the tried-and-tested methods, used by a country's advanced and intermediate enterprises, which can then be emulated by beginners or lagging MSMEs in developing and emerging economies.



Sharing best practices to enhance MSME ecosystem development

MSMEs in developed countries function in a far more organised and robust ecosystem compared to developing and underdeveloped economies. In view of this, establishing a network of practice-sharing between developed, developing, and under-developed economies is recommended.

Although each economy is heterogeneous and uniquely diversified, it can nonetheless benefit from replication of certain aspects of established practices with adjustments and customisations to account for its own context (for instance, demographic). To contribute towards the knowledge creation and to further increase economic value, governments of all established, developing, and emerging economies must become the principal practice-sharing partners through the alliance.

Implementation of policies and strategies

In comparison to large businesses that use tested and periodically modified strategies, MSMEs continue to struggle with a lack of effective and efficient

policies and strategies as well as the means to implement them, regardless of the state of the economy.

Complex policy and regulatory frameworks, global inflation, taxation issues, and the financial burden of having to comply with constantly changing regulations are hurdles for MSMEs.¹⁴ An International MSME Alliance can help Developing, LDC and LLDC governments to understand the simplification that can be brought in specific policies from experiences of developed economies, and the strategies that can be adopted and duplicated across regions. An International MSME Alliance can indeed play a crucial role in assisting governments in understanding policies and adopting effective strategies. Member governments within the alliance, particularly those that have made significant investments and policy interventions for the growth of their own MSMEs, can serve as guiding institutions for governments from underdeveloped and emerging economies. The member governments' successful experiences in simplifying policies, streamlining regulations, and implementing supportive measures can serve as practical examples for all policymakers.



Exchange of technical competence and MSME expertise

Innovation and contribution toward intellectual property are key indicators of an MSME industry's technological proficiency. MSMEs make up 20 percent of all patents in Europe, which is a significant portion given how rapidly innovation and economic value are being added, opening prospects for value sharing.¹⁵ Regardless of this, it is still difficult for entrepreneurs of low financial standing in developed economies or the MSME sector in underdeveloped economies to access key technical partners.

A global system with well-defined laws and regulations governing the exchange of technical competence and expertise will significantly enhance productivity and efficiency across all MSME and MSME-related sectors. This will also support the United Nations' Sustainable Development Goals (SDG 9), which calls for the growth of innovative industries as well as inclusive and sustainable industrialisation.

Inducting MSMEs into GVCs

Despite the role MSMEs play in employment generation and economic growth, they are largely still not substantially included in the GVC spectrum. The International MSME Alliance can be the most effective route to include the MSMEs of developed and developing economies into GVCs.

For the initial stage of this integration, there are two viable options: direct exports or direct forward participation through the export of intermediate products and services for well-established MSMEs with stable financial backing; or through indirect exports or indirect forward participation through supplying input products to local, and national, or multinational firms.

The challenges faced by MSMEs around the world are significant and diverse. Given that MSMEs are becoming the major drivers of economic growth and the largest employers in many countries, they will have a crucial role in realising the 17 SDGs. An international alliance whose main purpose is to



promote the expansion of the MSME sector globally will help achieve this goal. It will also give MSMEs worldwide an opportunity to collaborate, share best practices, and learn from each other's experiences. The International MSME Alliance, under the guidance of the G20, can establish a robust global MSME ecosystem, which will foster collaboration, knowledge exchange, and capacity building among MSMEs, ultimately leading to inclusive economic growth, job creation, and progress

towards the SDGs. Additionally, MSMEs in the alliance might be better prepared to deal with unforeseen disruptions, including economic crises and natural catastrophes (such as pandemics) by promoting risk management practices, fostering contingency planning, and exchanging expertise on business continuity. This preparedness can facilitate a quicker recovery, maintain sustainable operations, and help lessen the negative effects on MSMEs.

Attribution: Vinod Kumar Wuthoo and Maria Valeria Pasquini, "The Merits of an International MSME Alliance," *T20 Policy Brief*, June 2023.

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