

Giving SMEs a chance: lessons from Japan

IN THIS issue we carry a fascinating story of a small Mwanza-based firm that has proved in word and in deed that it is willing, able and ready to stand up to competition in its line of business.

The Nyakato Steel Mill produced less than 1,000 tonnes in its first year of operations in 1999. Today, the Mill produces 7,000 tonnes per year, and expects to hit the 10-12,000-tonne mark this year.

During that short period, its annual turnover has increased from Tsh300 million to Tsh2.8 billion today.

Furthermore, the foundry became the first mill in Tanzania to export steel products to neighbouring countries, making its first export to Kenya towards the end of 2003. It has also received orders from other countries, including Uganda, Rwanda, Burundi and the Democratic Republic of Congo.

Not only that. The company provides direct and indirect employment to scores of people in the Lake Victoria region.

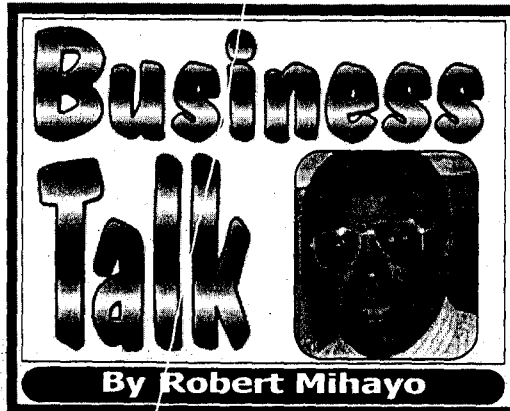
Indeed, the sky seems to be the limit for this nascent establishment. Well, not quite. High taxation, high power tariffs and generally poor infrastructure (among other drawbacks) threaten to bring this otherwise promising firm to a sad end.

Ironic as this may appear, it is some of the Government's own policies that enabled the Mill to be established in the first place. Yet, it is other policies of the very same Government that now threaten to bring it to its knees – unless corrective measures are taken soonest.

Quite sadly, what is most worrying is the fact that the problems of the Nyakato Mill are symptomatic of constraints other SMEs face in Tanzania and which stifle their full potential.

These constraints include an unfavourable legal and regulatory framework; undeveloped infrastructure; poor business development services; limited access to finance; an ineffective and poorly coordinated institutional support framework – and many more.

SMEs can play a crucial role in employment creation and income generation – not only in Tanzania, but in the world as a whole. Moreover, they can be easily established since their requirements in terms of



capital, technology and management are not that insurmountable.

SMEs can also be established in rural settings and, thus, add value to local agro products and, at the same time, facilitate the dispersal of enterprises.

In most countries, SMEs development is closely associated with more equitable distribution of income, which is important as regards poverty alleviation. They also serve as training grounds for emerging entrepreneurs.

Most people today are overawed by Japan's more-or-less miraculous industrial and technological might. And, to most outsiders, big manufacturers like Toyota Motor Corp., Sony Corp. and Matsubishi symbolize Japan's global economic might.

Often overlooked, however, is the abundance of small and medium-size manufacturers and their central role in production, even in such technologically advanced, internationally competitive product areas as motor vehicles and electrical machinery, as well as consumer and industrial electronics.

Indeed, very few people do realise that Japan's manufacturing sector was – and still is – highly dependent on the vitality of SMEs, which represent more than half of the value-added shipments from the manufacturing sector.

Statistics show that small and medium-size enterprises comprise about 99.4 per cent of all the establishments in Japan. The 80,000-plus businesses employ 71.5 per cent of the workers in the manufacturing sector. In terms of industrial shipments, SMEs account for 51.4 per cent of the total value, and 55.9 per cent of the value-added.

This illustrates very clearly the great contributions of SMEs to Japan's manufacturing sector, and their weight in the economy as a whole.

Contrary to predictions,

that SMEs would wither away as the economy matured, the reverse was the case, as they became deeply intertwined in the production networks of Japan's most competitive industries.

It would probably help to examine the historical development of SMEs, and how they came to occupy such an important place in the world's second-biggest economy.

SMEs were an important part of Japan's economic development almost from the start of the modern period. While small retail shops were quite numerous in what is known as the *Meiji Era*, their manufacturing counterparts only began to emerge in large numbers in the period following World War I.

They processed raw materials into finished consumer goods for the domestic and export markets. The firms often were part of production networks of mercantile capitalists who outsourced processing to less skilled labour in the poorer districts of big cities – and sometimes to master craftsmen working with apprentices in what primarily were craft industries.

They began to organize the production of machinery and other manufactured goods by small subcontractors who often owned factories that would handle more sophisticated production processes, and then assemble the final product.

But, these small manufacturing firms suffered from a severe lack of access to capital – which, in turn, restricted their profitability and stability.

This situation was perceived as a major problem to be addressed by the Ministry of Commerce & Industry, the prewar predecessor of the Ministry of Economy, Trade & Industry.

Subsequently, a series of laws were passed during the 1950s to help SMEs. These included the creation of special financing institutions (the *Small Business Finance Corp.*, formed in 1953), and

the protection of small firms from competition (the *New Department Store Law* of 1956).

Other measures included the reduction of taxes for smaller firms, as well as permission for SMEs to form commercial and industrial unions designed to prevent excessive competition and infiltration by bigger competitors (the *Small and Medium Enterprise Organization Law* of 1957).

Indeed, there was even enacted a law in 1957 – *Law of the Prevention of Delay in the Payment of Subcontracting Charges & Related Matters* – which prevented large firms from refusing to pay their subcontractors on time! That was the favorite way for big companies to shift costs to their SME partners.

The numerous policy initiatives targeted at SMEs finally were systematized with the enactment of the *Small & Medium Size Enterprise Basic Law* in 1963 that helped provide the necessary conditions for the continued growth and development of small manufacturers.

It aims to provide new paths for SMEs, and sets forth goals of policies for those enterprises.

For its part, the *Law on Supporting Business Innovation of Small & Medium Enterprises* stipulates measures to support business innovation SMEs in response to changes in the economic environment.

The law also provides measures to strengthen operating bases that contribute to future business innovation among SMEs which have been markedly affected by major changes in the economic environment. This promotes innovative development by small and medium enterprises, and contributes to the sound development of the national economy.

The *Small & Medium Enterprise Credit Insurance Law* sets small and medium enterprise credit insurance to facilitate the financing of operations for SMEs. Indeed, there is a plethora of laws in Japan that seek to nurse and nurture the SMEs sector.

It is such policies that have helped to transform what was a highly impoverished, backward nation barely 50 years ago into the second biggest economy in the world that it is today.

Let us here in Tanzania also give firms like the Nyakato Steel Mill a chance.