

Business Strategy of Small Medium Enterprises (SMEs): A Case Study among Selected Chinese SMEs in Malaysia

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Abstract: Small and Medium Enterprises (SMEs) in Malaysia particularly dominated by Chinese SMEs is acknowledged as a drive for economic growth and industrial development of the country. Despite the contributions made by the Chinese SMEs to Malaysian economic, very few studies, especially in relation to business strategy have conducted involving the Chinese SMEs. This study is therefore was embarked to explore business strategies of Chinese SMEs. Using Porter's five forces model, qualitative methodology in particular personal interviews have been conducted involving (15) owners of Chinese food manufacturing SMEs in Penang. Responses were analysed using MS Excel based on Miles and Huberman model. This study revealed that majority of the Chinese SMEs involved in this study have adopted more than one Porter's components as their business strategies. In fact, Porter's component found to be a complex framework and each component is interrelated from one to another. Among the five Porter's components, the substitution product found to be the most important component, followed by buyer's component. From this study, it can be concluded that the relative strength of Porter's components support in improving competitive advantage and identifying the optimal strategy under this competitive market. This study has provided better understanding on business strategy of SMEs in particular the Chinese SMEs in Malaysia.

Key words: Business strategy, Chinese SMEs, Porter's five force model, competitive advantage, optimal strategy

INTRODUCTION

The roles of Small and Medium Enterprises (SMEs) are significant in realization of long term business and industrial competitiveness of a country. According to United Nation's report on world economic situation and Prospects SMEs remain as one of the significant economic contributors in global. SMEs make up 99.8% of non-financial Enterprises, contributing 58% of region's Gross Value Added (GVA) and provided almost 67% of jobs. In Malaysia, the SMEs contribute a significant amount to economic development. Economically, in 2013 SMEs contribute 6.3% of Gross Domestic Product (GDP) compared to only 6% in 2012 (SME, 2013). As the SMEs become a major concern by most countries many strategies regard to the performance of the SMEs have been studies. For example a study from Bangladesh by Philip (2011) found that strategy has interrelation with business success. However, it was argued that although ways of doing business have significant positive impact of business success strategies do not

have significant influence to the success of any business (Chittithaworn *et al.*, 2011). In fact, many SMEs have not given attentions in developing effective strategies and most of the strategies formulated as short term goals or localized in functioning (Singh *et al.*, 2008).

In Malaysia to date very few studies that focusing on business strategy of the SMEs. As a consequences lack of an appropriate model that able to determine business strategy of the SMEs in Malaysia (Small, 2013). In fact to date no comprehensive framework in terms of policies and strategies towards SMEs development especially involving the Chinese SMEs in Malaysia (Saleh and Ndubisi, 2006). Therefore, it is valuable to explore this issue which can be adopted by new entrepreneurs to enhance their business. In addition, this study is also important for students professional and researchers to increase their knowledge on the related field.

Literature review

SMEs definition and development in Malaysia: In Malaysia, SMEs are grouped into three as Micro, Small

Table 1: Definition of SMEs in Malaysia

Category	Micro	Small	Medium
Manufacturing	Sales turnover of <RM300,000 or employees of <5	Sales turnover from RM300,000 to <RM15 mil or employees from 5 to <75	Sales turnover from RM15 mil to not exceeding RM50 mil or employees from 75 to not exceeding 200
Services and other sectors	Sales turnover of <RM300,000 or employees of <5	Sales turnover from RM300,000 to <RM3 mil or employees from 5 to <30	Sales turnover from RM3 mil to not exceeding RM20 mil or employees from 30 to not exceeding 75

and Medium. The latest SMEs definition launched on 1st April 2015 is based on two category, manufacturing and services and other sector according to the three groups, total sales turnover/revenue by a business in a year or number of full-time employees. The manufacturing sector SMEs for example is defined according to sales turnover not exceeding RM50 million or full-time employees not exceeding 200 (Table 1).

The development of Malaysian SMEs has been started as early as 1970s especially after the introduction of the New Economic Policy (NEP) in 1971. The NEP was aimed to improve the welfare and restructured the imbalance of economics within the ethnic groups in Malaysia. As a result of NEP a significant improvement of income distribution has been seen since 1990. The proportion of households incomes below the poverty line have been declined from 49.3% in 1970 to 16.5% in year 1990 and further decreased 5.1% in 2002 (Economic Planning Unit, 2014).

The establishment of Small Medium Industrial Development Corporation (SME Corp) on 2nd May 1996 was the main effort by the government that focus on SMEs development of the country. SME Corp suggested five strategic thrusts that concerned about SMEs development especially in the manufacturing and services industry: enhance the SMEs competitiveness, encourage SMEs look outward capital investments, drive of SMEs via technology and innovation knowledge, instituting more cohesive policy and supportive regulatory or framework (SME Master Plan, 2012-2020). In year 2010, the government formulated the Economic Transformation Programme (ETP) that focusing on achieving on high income status country by 2020. The ETP is targeting an average annual growth in Gross National Income (GNI) of 6% with percapita income from RM 23700 in year 2009-RM 48000 in future year 2020. SMEs are expected as part of the catalyst of the ETP since SMEs are addressing the bottom 40% of national income of the country (SMEs Master plan 2012-2020). The new strategy in fact is encapsulated in SMEs Master plan (2012-2020) as a critical guideline for SMEs policy direction and for the next nine years. The plan is developed to increase market access and infrastructure development of SMEs in Malaysia, especially to build strong base of vibrant and competitive SMEs to face the challenges arising from this dynamic markets.

Business strategy: Strategy is defined as a plan that designed for special purpose or planning and managing any unfair well plan. In term of corporation, strategy is a comprehensive plan for the corporation to attain its mission and goal. Hirsh explained that concept of strategy was different from mission, goals or plans. Specifically, business strategy is the decision making process that take place in business to improves the products in order to sustain firm's competitive position or service in particular industry or market segment that present in business (Campbell *et al.*, 2002). Hence, business strategies usually composed of competitive and cooperative strategies such as differentiation competitive strategy for innovation products or cooperative strategy to form an alliance and so on Hunger and Wheelen (2007). Nickols stated that business strategy is very complexity since its required various logically thoughts, ideas, experience, knowledge, expertise and more before achieve desired outcome. In short, business strategy can be considered as long term plan to achieve strategic goals. As strategy interaction is very complex any organizations are required to have clear understanding and proper precondition to shaped strategy in order to accomplish their goals. In general, strategy is the significant framework that leaded the action to be taken and usually designed by executive management for the purpose of gain long term value in business.

Porter's five forces: It is argued that business model and strategy are related but both are different constructs that have been designed in different mechanisms. In order to sustainable in this globalization it is very critical for any company to formulate a well-designed business model (Casadesus-masanell). There are several popular business models developed throughout the world. The most popular model such as SWOT analysis, Balance Scorecard, Porter's five forces model and much more. This study focused on Porter's five forces model as it provides a complete components of strategy as well as relevant to any business environment including Malaysia SMEs.

Porter's five forces model (Fig. 1) can be applied in any sectors of economy. Porter (1998, 1985) introduced the five competitive forces impact and collectively defined the overall profit potential in an industry. The five

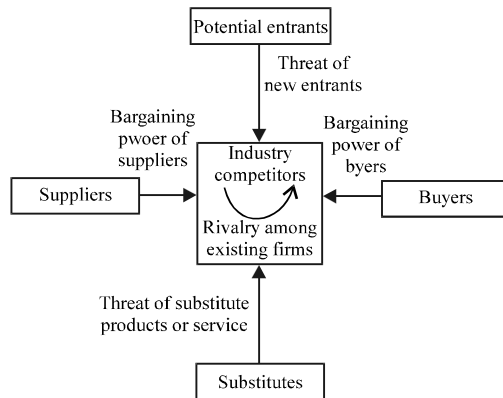


Fig. 1: Porter's five model

competitive forces components include potential entrants, substitute products or services, buyers, suppliers and industry competitors.

Potential Entrants (PE): A market would attract a new entrant when the existing businesses are profitable. However, the barriers to entry can be created by the government by the nature of business, existing companies, industry structure (Entrepreneurial Insight, 2014) and capital structure (Chiang *et al.*, 2010). The threats of new entrants to enter the industry depend on many factors include: brand loyalty of customers; initial capital costs, fixed costs, capital required, protection of intellectual property, customers switching costs; cost advantages; economics of scales; scarcity of resources; access to raw materials and the Government regulatory and legal constraints (Porter, 1985, 1998; Campbell *et al.*, 2002; Wilkinson, 2013). For example, the difficulty in obtaining raw materials from suppliers will eliminate new entrant opportunities.

Substitution Product (SP): The substitution illustrated the company's products can be replaced by other different products (Porter, 1998). The threat of substitute's products potentially attract a significant proportion of market volume and influence the decision of pricing mechanisms and profitability of a company (Lus and Muriel, 2008). The threat of substitutes product usually in a high risk due to a number of reasons such as when consumer switching cost is low, substitute product is cheaper than industry product, quality is equal or superior or substitutes performance (Hines, 2013). Further, the threats of substitution products or services depend on several factor such as availability of substitute's products, quality of substitute's products,

switching cost for customers, brand loyalty of customers, close relationship between customers, current fashion, trend and the relative price for performance substitutes (Campbell *et al.*, 2002; Wilkinson, 2013). Thus, the companies should reduce the effect of substitution products by increasing variety and broad products (Koo *et al.*, 2011) as well as undertake the consumer's behaviour (Lattin and McAlister, 1985).

Buyer (B): The buyer purchasing power can be reduced when a large number of similarity supplier compared to the buyers. In fact, bargaining power of buyers tend to be higher when product is undifferentiated and easily be replaced by substitutions. It was argued that customers will easily losing their brands loyalty if there is little differentiation of products. The influence of buyers may also reduce profits of the sellers through reduction of price, improvement of customer service or delivery order or influence other sellers (Valuation Academy, 2010). Further, the bargaining power of buyers likely to be high on, concentration of buyers, supplier operate in high fixed costs, products is undifferentiated, switching cost is low and simple, customers have low margin, price sensitive, the products is not extremely important to the customers, customers could produce the products by themselves, customers know the cost of production and the potential for customers integrate backward.

Supplier (S): Supplier's power refers to the pressure that suppliers can exert on businesses. It was argued that supplier power can influence price of the target market, the quantity and quality available to purchase and even to sustain in the marketplace. A strong supplier can make an industry more competitive or reduce the profit potential for the buyer (Wilkinson, 2013). The Open University stated that the relative strength of supplier is influenced by the forward integration strategy. If there is a strong alliances between buyers and suppliers, the relative strength of the remaining suppliers will be less. Further, the bargaining power of supplier likely to be higher when few dominant suppliers, no substitutes for particular input and the supplying industry has a higher profitability than the buyer industry (Campbell *et al.*, 2002; Hunger and Wheelen, 2007; Mars, 2014).

Industry Competitors (IC): The intensity of rivalry among competitors in the industry refers to the extent to which company put pressure on one to another company within the industry power (Wilkinson, 2013). According to David (2011) in a high intensity of rivalry, competitors will be

very aggressive targeting to each other's markets and pricing products and finally decrease profit potential for the existing firms. The industry rivalry usually contended their market position using various strategies or tactics such as price competition, advertising battles and product introduction (Mars, 2014). Further, the intensity of rivalry among competitors in the industry will be higher if there is a lot of small or equally size competitors as well as little products differentiation between competitors (Campbell *et al.*, 2002; Peters, 1997).

MATERIALS AND METHODS

This study employed a qualitative method since this method found to be the most suitable method to capture new issue that not yet explored. The purposive sampling involving fifteen owners of Chinese food manufacturing SMEs in Penang. Penang has been chosen as location of the study since the industrial sector in Penang account for 88% of the manufacturing and manufacturing-related services. Personal interviews had been chosen as a primary data collection technique using semi-structured questionnaire. The data gathered from the interviews were organized and analysed using Miles and Huberman (1994) model. The data reduction was conducted to filter the information which is related with the researcher's research question and organized business strategy information that match to researcher's objectives which related to Porter's Five Force Model.

RESULTS AND DISCUSSION

Company background: The summary for companies' backgrounds involved in this study is displayed in Table 2. The companies have been established as early as year 1975 until 2012. The companies are involved in food manufacturing such as processed food, frozen food, biscuit and bakery and others.

Business strategy: The responses rates on business strategy adopted by the companies is shown in Table 3. The indicated that that each company has almost the same priority weight on the Porter's components. After integrating the priority weight of responses rates, the highest rate was the Substitute's Products (SP) (15), followed by buyer-Buy (12). While the supplier (S) and Industry Competitors (IC) has equally rates of 7, finally, the component of Potential Entrant (PE) was the lowest rate (6) among all the components. Therefore, it can be concluded that substitution product is the most important component of Porter's business strategy adopted by the Chinese SMEs in Malaysia.

Table 2: Company's background

Company	Year of establishment	Company's products
1	2010	Traditional vegetarian pastry, pau, traditional food and etc
2	1995	Penang famous Tambun Pau Biscuit and etc
3	1996	Processed frozen foods such as Almond Bun, Chicken roll, Chicken Dim Sum and etc
4	1975	Coffee products, tea products, curry powder products
5	1983	Biscuits, snacks, mooncake and etc
6	2012	Bakery and cake products such as butter bun, tuna fish, donut, puff, butter cake and etc
7	2008	Frozen seafood products such as fish ball, dumpling and etc
8	1996	Biscuits and bakery
9	2001	Processed frozen foods
10	1980	Bakery and cake products
11	1992	Processed frozen foods
12	2001	Frozen seafood products
13	1998	Bakery and cake products
14	2002	Frozen seafood products
15	1995	Biscuits, snacks

Table 3: Company's business strategy based on porter's five force model

Company	Number of strategy				
	Buy	S	SP	IC	PE
1	✓		✓	✓	✓
2	✓	✓	✓		✓
3	✓		✓		
4	✓	✓	✓	✓	✓
5	✓	✓	✓	✓	
6	✓	✓	✓		✓
7			✓	✓	
8	✓	✓	✓	✓	
9			✓		
10	✓		✓	✓	
11	✓	✓	✓		✓
12	✓		✓	✓	✓
13			✓		✓
14	✓	✓	✓		
15	✓		✓		
Total	12	7	15	7	6

It is also discovered that although the Substitution Product (SP) component was the main Porter's component, the component is interrelated with buyer component. This can be explain because most customers usually prefer better quality product with lower price. Hence, Majority of the companies highlighted that good product and service are the key factor to satisfy customers, followed by the adorable or low price since the customer are usually price sensitive and reduce their purchase power especially when product are undifferentiated or easily replace by other similar products. As Chen (2008) mentioned buyer have bargaining power to affect the decision of companies in setting price of a product. The impact of substitution products have influence the decision of pricing

mechanism and determine profit of a company (Lus and Muriel, 2008). Apart from that all companies in this study produced multiproduct in order to fulfil the market demand. This can be explained because companies have produced broad, variety or different products to reduce the impact of substitute's products in the market (Koo *et al.*, 2011). In addition, variety of products is needed to fulfil the determination from the customers (Lattin and McAlister, 1985). Recklies demonstrated that there are other underline factors such as lower shifting cost and fashion trend might shift the customer preference. Hence, some companies in this study had set low price as their marketing strategy in order to be more competitive in the marketplace. Similar to WESP (2013) this study found that buyers and suppliers component are interrelated. Luxinnovation stated that buyers bargaining power tends to be inversely proportional to the suppliers. Hence, in accordance with Berman many SMEs in this study illustrated that good communication and relationship among suppliers can gain cost advantage in input resources since the supplier pressure can influence cost, quantity, quality of available resources and raw materials.

The research point out that there are many reasons for potential entrants includes high potential market, nature of business in food manufacturing industry, demand of customer increase, attraction to be successful entrepreneur. While some of the companies supported capital structure (Chiang *et al.*, 2010) such as low entering cost, high return margin, the fast return in investment was the reasons that make outsiders enter to the same industry. The cost in fact can influence the difficulty of new entrant to established especially they faced obstacle in searching appropriate suppliers to obtain raw materials (Market Watch, 2011).

This study concludes that to formulate business strategies, the company should use more than one component of Porter's five forces model. Further, all five components of Porter's model (buyer, supplier, substitute product, industry competitors and potential entrance) are interrelated from one to another. Hence, the finding supported Hornby (2010) who concluded that Porter Model always work effectively and interrelated to each other. This interrelationship framework occurred when one component was influenced by other components. Based on the findings the Porter Model is attempted to move the understanding on simple market or a static economic market which are less of uncertainty and then emphasis on the interdependence of forces as dynamic or punctuated equilibrium. Some criticism of doubtful assumption explored that buyers, competitors and suppliers are separate entities that never interact, never

collude and never influence each other directly. As a conclusion, this study discovered that all Porter's components influences the state of competition in any industry and most components are interrelated in conducting business strategy.

CONCLUSION

The study outlining that most components in the Porter's five force are interrelated. A company might use more than one component to plan, organize, formulated their business strategy mechanism. In fact to sustain in the market, the company need more than one Porter's component as the business strategy. The pressure form substitute product is the most important consideration for the SMEs in this food manufacturing industry. The study provided new information regarding business strategy based on Porter's five force model to the Chinese SMEs. Future study can be done to be applied in other industry among SMEs, specifically using quantitative method or a mixed research method. Hence, the future results can provide additional information and give more weight to the themes established in this study.

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