

# SME and FDI Policies in East Asia



Malaysian Industrial  
Development Agency



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## Topics

- QCD of Japanese enterprises
- Supporting industries
- Success factors in industrial parks
- Country evaluations by Japanese FDI
- Malaysia's Manufacturing++ and cluster-based approach
- SME policies of Malaysia, Thailand
- Policy Proposals for Vietnam

## Quality, Cost, Delivery (QCD)

- Japanese manufacturers pursue **QCD** for competitiveness.
- They also demand **QCD** from suppliers.
- **Q** means zero defects (all problems solved within factory, never shipped to customers).
- **C** means cutting cost (subject to **Q**)
- **D** means on-time delivery and no (excess) inventory. It was spearheaded by Toyota's *just-in-time* system. Logistics is also key for quick delivery.



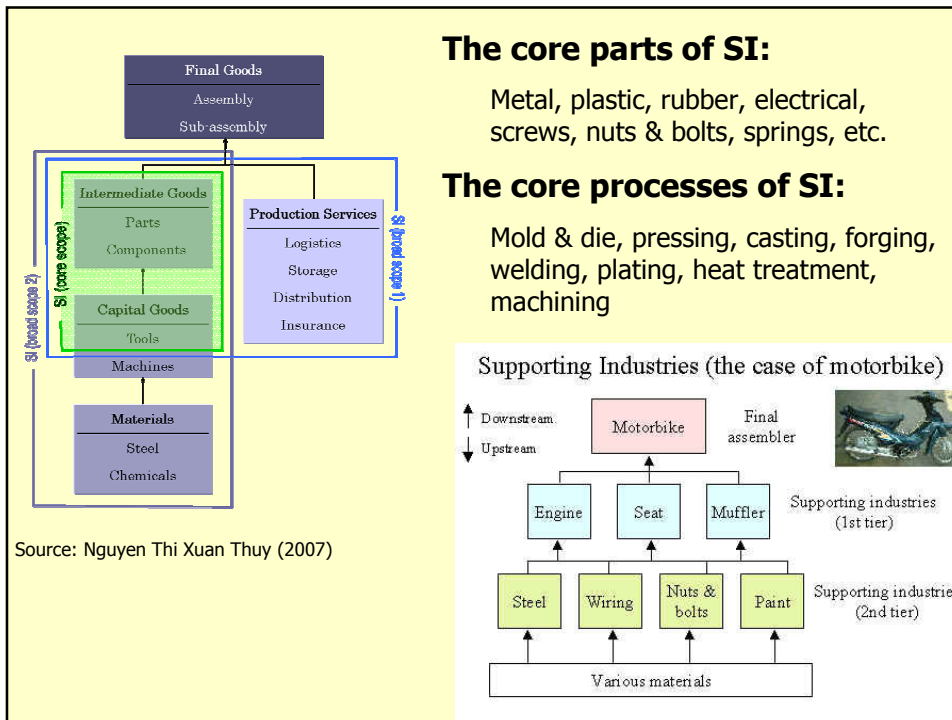
A panel inside a Japanese FDI factory in Hanoi, Vietnam

### The Pledge of Monozukuri (Manufacturing)

- 1. Keep Delivery Date**  
--It is our responsibility
- 1. Guarantee Quality**  
--It is our pride
- 1. Cut Cost**  
--It is our duty

## Supporting Industries (SI)

- “Supporting industries” refers to parts industries for mechanical assembly such as electronics, cars, motorbikes.
- Development of SI is key to competitiveness, since 80-90% of production cost is parts cost.
- The term “Supporting Industries” has been used by Japanese government since mid 80s.
- Similar terms: parts & components, suppliers, vendors, subcontractors, ancillary industries.



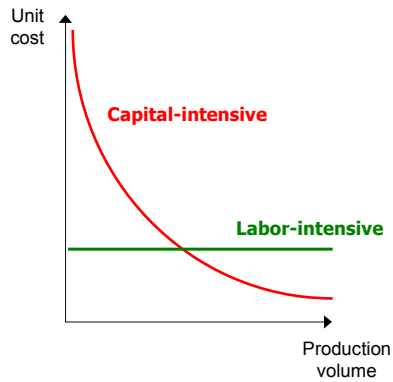


## Why is Demand Size So Important?

Generally, supporting industries are more capital-intensive than final assembly

- Large investment in equipment (indivisibility)
- Unit cost declines inversely with production volume

“Supporting industries will develop naturally, even without promotion policy, if demand size is sufficiently large.”  
 – an auto parts supplier.

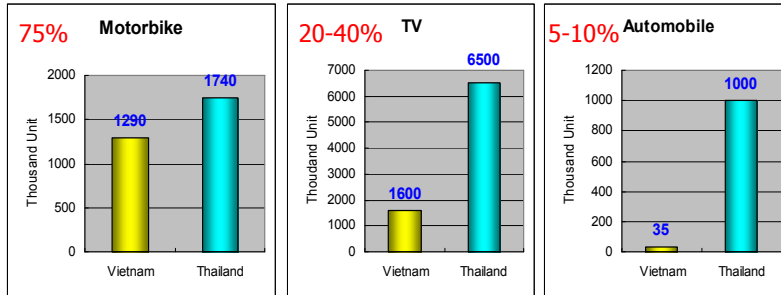


## Limited Demand Size in Vietnam

The larger the demand size, the higher the local procurement ratio.

**Motorbikes > E&E > Automobiles**

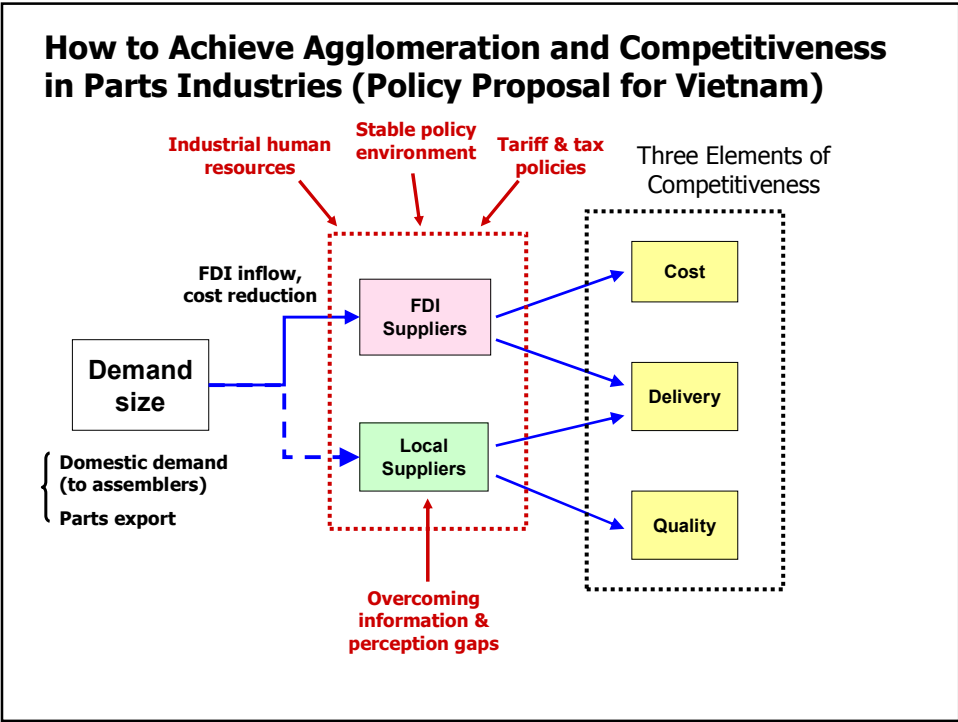
**Localization ratio in Vietnam** <Production-size comparison: Vietnam vs. Thailand>



Data for 2003 (Mishima)

Data for 2002 (GSO, New Net Asia)

Data for 2005 (VDF-MOI hearing)



## Ingredients for Successful Industrial Estates

Mr. Hajime Yamaguchi (Sumitomo Corp.), creator of two successful industrial parks in Indonesia and Vietnam:

Success ingredients are:

1. **Good location** (access to urban center, port, airport)
2. **Good infrastructure service** (power, water, waste treatment, etc)
3. **Good management** of industrial estate (pre- and post-investment support)



## FDI Policy: Centralized vs. Decentralized

- Thailand (BOI) and Malaysia (MIDA) have centralized FDI policy, marketing and approval systems (2-3 zones within country, but no local incentives)
- Vietnam has decentralized FDI approval and marketing (provincial level).
- China: built-in local incentive to attract FDI and over-invest; less attention to quality or environment.

## JBIC Survey of Japanese FDI

- Japan Bank for International Cooperation (JBIC) conducts annual survey on Japanese multinational firms. In 2005, 590 firms were surveyed.

Where do you plan to expand business in the next three years? (Multiple answers)					
1	China	82%	8	Indonesia	9%
2	India	36%	9	Brazil	7%
3	Thailand	31%	10	Taiwan	7%
4	Vietnam	27%	11	Malaysia	5%
5	United States	20%	12	Mexico	3%
6	Russia	13%	13	Germany	3%
7	Korea	11%	14	Philippines	3%

### China (perception of Japanese FDI, 2005)

#### MERITS

Large domestic demand	68.8%
Cheap labor	58.1%
Large parts supply	31.2%
Export base (to world)	28.0%
Industrial agglomeration	21.5%
Export base (to Japan)	21.5%
Cheap materials	20.4%

#### DEMERITS

Unpredictable laws	60.7%
Violation of intellectual property	49.4%
Severe competition among rivals	44.9%
Wage increase	42.7%
Exchange control	41.6%
Social unrest	39.3%
Unpredictable taxes	34.8%
Unrecoverable payments	32.6%

### Vietnam (perception of Japanese FDI, 2005)

#### MERITS


Cheap labor	79.5%
Human resources	38.6%
“China plus 1” (*)	31.8%
Future potential of domestic market	29.5%
Export base (to Japan)	20.5%
FDI incentives	20.5%
Export base (to world)	15.9%
Political stability	11.4%

#### DEMERITS

Poor infrastructure	55.9%
Undeveloped laws	38.2%
Unpredictable laws	38.2%
Poor logistics and transport	35.3%
Poor supporting industries	29.4%
Lack of information	26.5%
Unpredictable taxes	17.6%
Lack of middle managers	17.6%

(\*) Diversification of investment risk by investing in countries other than China.

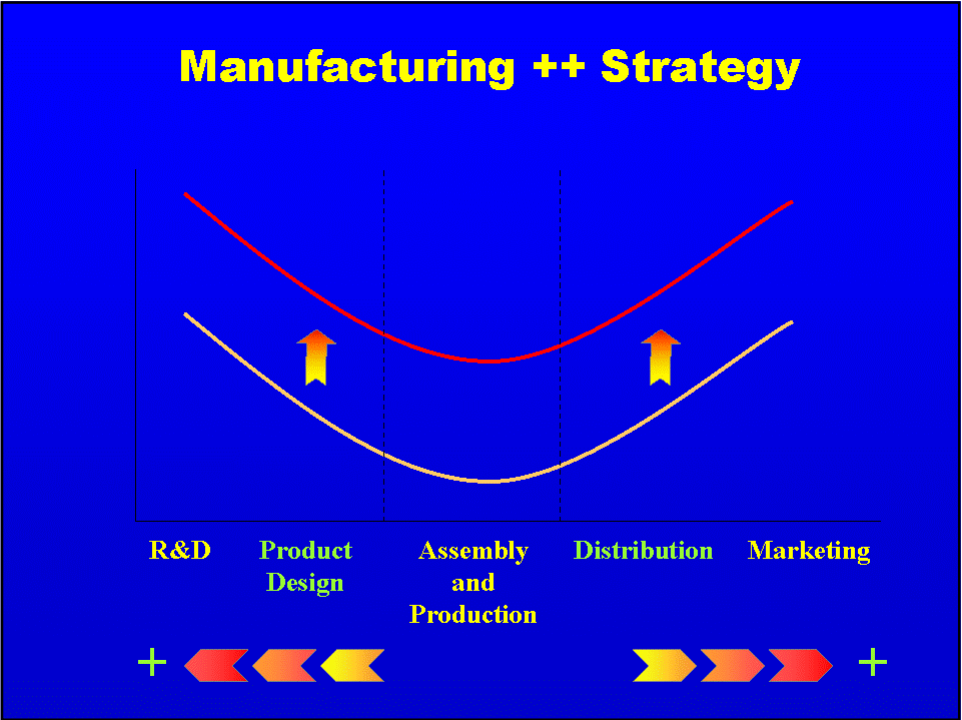


  
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## MAIN FOCUS OF IMP2 (1996-2005)

- Manufacturing *Plus Plus* Orientation
- Cluster-Based Industrial Development

Excerpts from the slides on  
Industrial Master Plan 2 (1996-2005)  
by Malaysia's Economic Planning Unit (EPU)  
Presented to VDF delegation, January 2006





## Twin Strategic Thrust of *Manufacturing Plus Plus*


- Move Along The Value Chain Towards Higher Value Added Activities
  - R&D and Product Design Emphasis
  - *Services, Distribution and Marketing Emphasis*
  
- Shift The Whole Value Chain To a Higher Level Through Productivity-Driven Growth
  - Higher Technology Utilisation (Automation/Robotisation)
  - *Increase Total Factor Productivity (TFP)*



## Cluster-Based Industrial Development

### KEY ELEMENTS

- Identification of Clusters
  - *Enhancing Value Added and Value Chain*
  - Identifying and Developing Key Suppliers
  - *Strengthening Economic Foundation*
- IT IS IMPORTANT THE 4 ELEMENTS TO BE IMPLEMENTED SIMULTANEOUSLY



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## CLUSTER-BASED INDUSTRIAL DEVELOPMENT

- Key Elements
  - A Cluster is an agglomeration of key industries – suppliers, critical supporting sectors & services, infrastructure & institution
  - Companies form partnerships with supplier & competitors to increase value added activities i.e. common labour pool
  - Companies form strong links with local R&D institution to strengthen product development & design capabilities
    - Outside the cluster, the companies are connected to a global network of subcontractors & vendors



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## CLUSTER-BASED INDUSTRIAL DEVELOPMENT

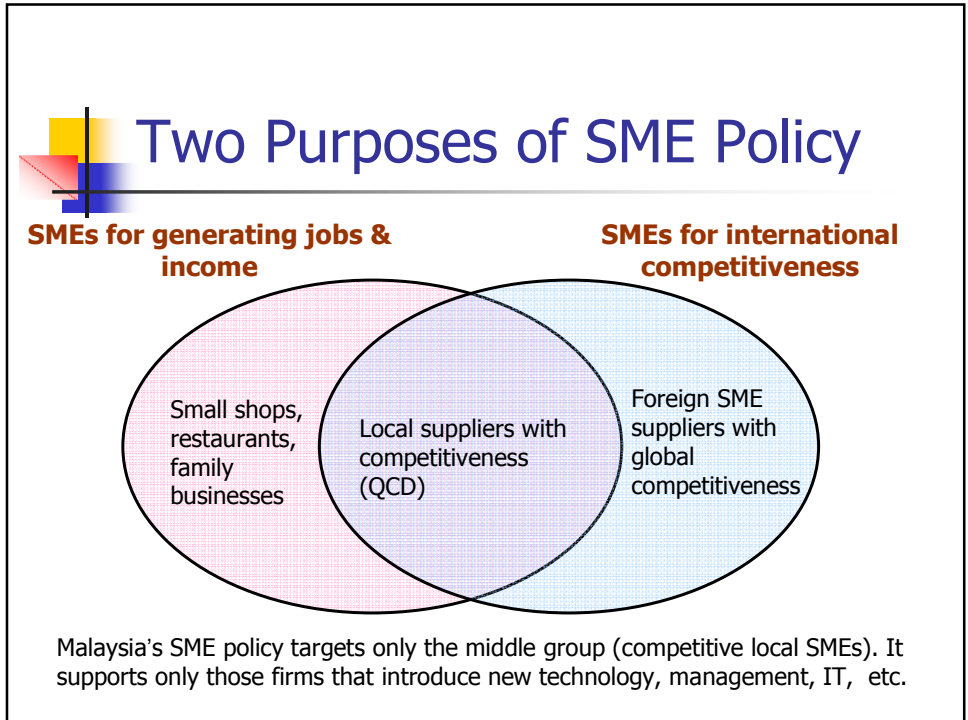
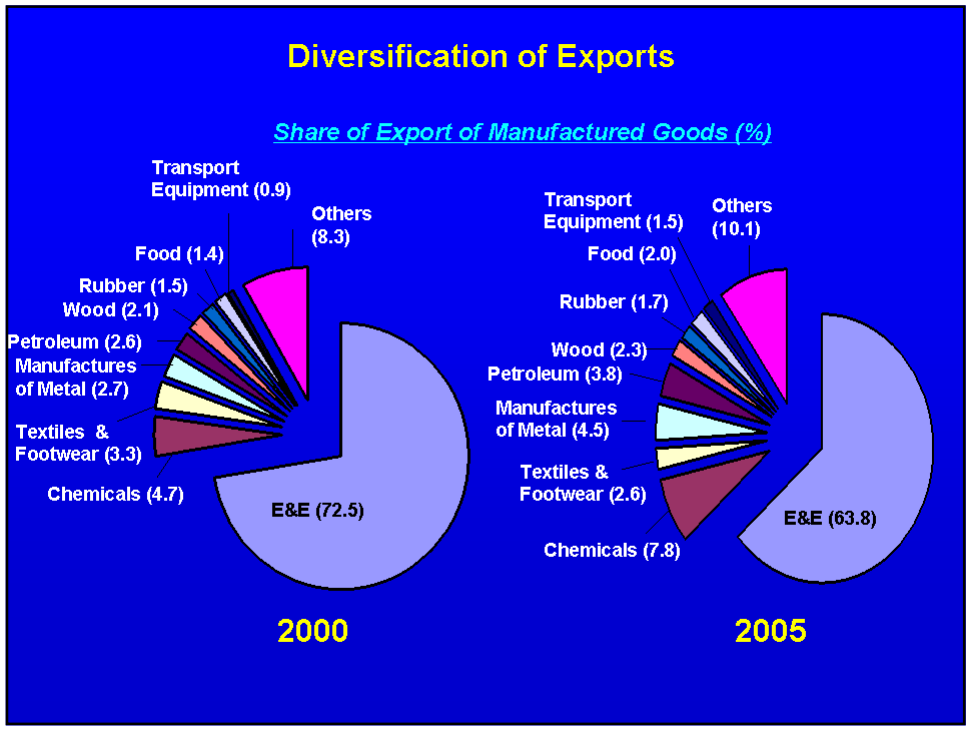
- Cluster-based Industrial development need to be supported by the requisite economic foundation;
  - Human Resource
  - Technology
  - Physical Infrastructure
  - Business Environment

## Industries To Be Developed On A Cluster-Based Approach

- Electrical and Electronics
- Textiles and Apparel
- Chemicals
- Resource-based Industries (Rubber and Wood)
- Agro-based and Food Products Industries
- Transportation
- Materials and Advanced Materials
- Machinery and Equipment

## Major Indicators of Manufacturing Growth

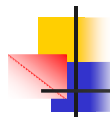
Major Indicators	1996-1998	1999-2000	2001-2003	2004-2005
Value Added (RM mil) <sup>1</sup>	140,109	93,740	199,479	156,900
Annual Growth Rate (%)	4.3	3.4	1.5	7.8
Share to GDP (%)	34.8	34.5	30.3	31.4
Share to Total Exports (%)	81.5	84.5	84.2	83.6
Share to Total Employment (%)	26.9	27.2	27.3	28.9





## Common Policy Measures

- Local content regulations (no longer allowed under WTO)
- Attraction of FDI suppliers
- FDI-local linkage promotion
- Incentives (targeted, conditional on effort/action)
- Assist participation in global production networks



## Vendor Development Program (Malaysia, 1988-97)

- Large FDI firms (“anchors”) were asked to nurture local vendors (first-tier suppliers & Bumiputra firms).
- Interest-free loans were provided to participating local firms.
- *Not very successful due to low capability of local firms, unwillingness of FDI firms.*
- Later, replaced by Industrial Linkage Program (ILP, 1997-). Candidates were expanded to second-tier suppliers and non-Bumiputra firms also.




### Small and Medium Industries Development Corporation (SMIDEC) (Malaysia, 1996-)

- Eligibility—local capital >60%, annual sales <RM25m, employees <150; manufacturing, manuf. services, agro business
- **Grants** for business planning, product & process improvement, marketing, certification, improved packaging, design, labeling, etc.
- **Soft loans** for factory relocation, ICT, etc.
- Quick disbursement with monitoring; must return money if plans are not implemented.
- Match-making database of 18,000 firms
- FDI-local matching, 250 cases per year



### BOI Unit for Industrial Linkage Development (BUILD) Program (Thailand, 1992-1997)

- Targets: electronics, cars, machinery
  - Database for company matching
  - Training local suppliers & seminars
  - Trade fairs
- Not successful due to lack of recognition, needs study, coordination among organizations**
- Subsequently, JICA was asked to draft master plan on development of supporting industries.



## Proposed SI Measures by Motorbike Joint Working Group (Vietnam, May 2007)

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- M1**—Incentives for investment and training  
Tax & tariff exemptions and training subsidies  
for pressing, casting, forging, welding and  
die-and-molds
- M2**—Mechanism for receiving foreign experts  
Needs matching, assist life & work of foreign  
experts; invite retired engineers from Japan
- M3**—Strategic FDI marketing  
Shift from general to targeted marketing;  
attractive industrial parks and rental factories



## Vietnam (cont.)

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- M4**—Database  
Start with small size and expand later;  
database and company matching must be  
integrated
- M5**—Technical education and training  
Establish/support a few pilot schools and  
disseminate nationwide
- M6**—Testing centers for motorbike parts  
Create new centers and strengthen existing  
ones; TA and equipment should be provided