



Briefing Paper

Initiative to Enhance MSME Participation in International Trade

Challenges and Opportunities in the Context of the WTO

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Summary

In recognition of the role performed by MSMEs in many economies, a group of WTO Member countries through a Joint Ministerial Statement at the 11th Ministerial Conference of Buenos Aires, established an Informal Work Programme (IWG) for MSMEs. The informal working group seeks to achieve horizontal and non-discriminatory solutions so as to yield benefits for the participation of MSMEs in international trade, considering specific needs of developing countries and LDCs. This briefing paper summarises findings from a recent CUTS study which highlights the challenges and opportunities for promoting integration of MSMEs in international trade.

Introduction

It is acknowledged that Micro, Small and Medium Enterprises (MSMEs) play a significant role in economic development of countries, more especially developing countries and Least Developed Countries (LDCs) where they employ majority of the workforce in both the formal and informal sectors, serve as incubation phases of enterprises, and contribute to value chains of all economic sectors among other attributes. To foster inclusiveness in trade and development, Governments at national, regional and international level are increasingly directing policy attention to enhancement of MSME participation in economic and trade activities. At the apex, the Sustainable Development Goals (SDGs) acknowledge the potential for MSMEs in contributing towards their attainment, specifically by promoting inclusive and sustainable growth, full and productive employment and decent work for all.

From the foregoing, and in recognition of the role performed by MSMEs in the national economies of WTO Members, and which is not commensurate with their share in international trade, a group of Member countries through a Joint Ministerial Statement at the 11th Ministerial Conference of Buenos Aires, established an Informal Work Programme (IWG) for MSMEs.¹

The informal working group seeks to achieve horizontal and non-discriminatory solutions so as to yield benefits for the participation of MSMEs in international trade, considering specific needs of developing countries and LDCs. According to the Declaration, the overarching objective is to address obstacles related to foreign trade operations that represent a significant burden for MSMEs interested

in participating in international trade.

This briefing paper summarises findings from a study on “Enhancing the Participation of MSMEs in International Trade: Issues and Recommendations in the Context of WTO” so as to highlight the challenges and opportunities for promoting integration of MSMEs in international trade.²

The MSMEs Initiative in the WTO

The MSMEs Joint Statement agreed at the Eleventh WTO Ministerial Conference of 2017, was a culmination of discussions and events held on the issue, including at an Aid4Trade review session that focused on MSMEs.

The Joint Statement resulted in establishment of an Informal Working Group (IWG) on MSMEs that is open to all WTO members. Informal discussions are aimed at finding alternative instruments that would enhance participation of MSMEs in international trade. Presently, pursuing a binding multilateral agreement on MSMEs is unlikely given divergent views amongst WTO Members, who although acknowledge the vital potential of MSMEs, differ on the approach and role of the WTO on the issue. Agreeing a plurilateral agreement or some form of non-binding “soft law” seems a more likely outcome of the MSMEs initiative in the WTO.

Meetings of the informal working group (IWG) on MSMEs during 2018, were mainly to exchange information and for experience sharing, so as to gain more insights on the issue. The discussions revolved around the following themes: transparency, access to information, trade and finance issues for MSMEs, technical assistance and capacity building initiatives,

¹ WT/MIN(17)/58

² Full study is available at <https://goo.gl/QWiqHY>

and technological innovation and the internet as a tool to access global markets.

Going forward, a standing agenda was proposed that would work towards: 1) achievement of concrete deliverables; 2) expansion of the group membership; and 3) securing commitment by Ministers towards a Ministerial Declaration at the next Ministerial Conference.³

With regards to the ambition of achieving concrete outcomes, three paths are proposed along which deliverables could be discussed:

- First, thinking along *trade thematic deliverables* could aim at ‘ensuring that trade rules are conducive to MSMEs integration in regional and global value chains. Under this analytical strand of work, issues proposed for further investigation by the Secretariat include Trade Policy Reviews (TPRs), mapping national trade finance programmes and *de minimis* [in e-commerce]. Reviewing relevant MSME discussions in other WTO Committees, and preventing overlap and duplication with other WTO Committees is equally proposed as a focus of work for the coming year.
- Second, the theme of *technical assistance and capacity building* was a recurring theme, to ensure that smaller firms are actually able to participate in international trade (as for example discussed during the ITC-WTO Workshop on ‘Enabling MSMEs to participate in international trade’ in June 2016⁴).
- In addition, the third theme of *transparency*

and outreach / coordination appeared as frequently mentioned theme. Here, consensus on the need for more active engagement with the private sector seems to exist, and the proposal for regular meetings with representatives of the private sector was proposed.

Challenges and Opportunities for MSMEs in International Trade

There is a discrepancy between MSMEs contributions to domestic economies and their role in international trade. The 2016 WTO World Trade Report ‘Levelling the playing field for MSME’s, which aimed to support an informed discussion on MSME’s in WTO context, found that:

- Whereas MSME contribution to domestic economies and employment is high, the participation of MSMEs in (global) trade is weak. For example, *direct exports* represent only 7.6 per cent of total sales of MSMEs in the manufacturing sector, compared to 14.1 per cent for large manufacturing enterprises. Among developing regions, Africa has the lowest export share at 3 per cent, compared to 8.7 per cent for Developing Asia.
- Participation by MSMEs in direct exports of services in developing countries is negligible, representing only 0.9 per cent of total services sales compared to 31.9 per cent for large enterprises. In all, the direct trade participation of MSMEs in developing countries is not in line

³ Informal working Group on MSMEs: End of year wrap-up session: Summary of discussions, 6 December 2018, WTO Reference doc: JOB/GC/209

⁴ ITC news item on ITC-WTO workshop on ‘Enabling MSMEs to participate in international trade’, organized along with missions

of Philippines, Lao PDR, Malaysia, Brunei Darussalam, Singapore and Thailand (21 June 2016), see: <http://www.intracen.org/news/Enabling-MSMEs-to-participate-in-international-trade/>

with their importance at the domestic level.

- Research based on World Bank Enterprise Surveys showed that the ability to internationalize differs by region and by sector. For MSMEs in developing Asia, it took on average less time to start exporting compared with a firm of the same size in Africa or in Latin America.
- The longest time lag to export was found in the food sector, on average more than 14 years, twice the time necessary to begin exporting in the textiles and garments or office equipment and electronics manufacturing sectors.
- Compliance with sanitary and phytosanitary standards (SPS) and technical barriers to trade standards (TBT) appears to be a key challenge for MSMEs in the food sector explaining the longer time lag needed to transition into export.
- Internet-enabled MSMEs are an exception to the rule of low trade participation, with very high rates of exporting approaching 100 per cent⁵.
- Another finding is that MSMEs frequently opt for '*indirect trade*' strategies as a step to internationalize, confirming the importance of global value chains (GVCs). Direct trade (occurring when a company sells goods or services directly to customers in another country) is in that sense often perceived as entailing burdensome costs regarding trade compliance and business development (finding clients in target markets etc). This leads

MSMEs to opt for '*indirect trade*' strategies . Exporting indirectly is considered a less risky step to reach the international markets, as compliance and business development costs are born by the direct trader.

- Measuring the importance of MSMEs' trade in global value chains (GVCs) remains a challenging task, especially when it comes to mapping indirect participation of MSMEs in trade, for example, where an enterprise provides intermediate or final goods to a domestic enterprise that exports. However, data sets on developing economies confirm that indirect exports also show a discrepancy between MSMEs (2.4 per cent of total sales) and large manufacturing enterprises (14.1 per cent of total sales). Whereas in Africa both large firms and MSMEs are largely cut off from GVCs, the report mentions that even in Developing Asia most manufacturing MSMEs have both low forward and backward GVC participation rates compared to those of large enterprises⁶.

Whether MSMEs manage to export directly or indirectly, and move up the value chain depends to a large part on whether they are globally competitive in their chosen business activity. As mentioned in the MSME Competitiveness Outlook 2015: 'the recipe for successful MSME internationalization is likely to boil down to the determinants of MSME **competitiveness**⁷. Whether or not an enterprise is competitive in international markets equally depends on the capacity to deal with the challenges of trade. For MSMEs, these challenges are directly related to their size, and also are amplified when set

⁵ WTO World Trade Report, 'Levelling the trading field for MSME's, WTO, 2016, p. 54

⁶ WTO World Trade Report 'Levelling the trading field for MSME's, WTO, 2016, p. 6

⁷ ITC MSME Competitiveness Outlook 2015, p. XVII

in a global context.

Challenges

Challenges faced by MSMEs can be categorized as those faced at firm-level on the one hand, and those resulting from policy and the business environment they operate in, on the other.

At firm-level, larger firms are more likely to export than MSMEs, in part due to the fact that they are more productive and as a result also pay higher wages (attracting higher educated workers). Firm level capability and capacity is crucial for firms' success; from managers' ability to the technology tools available in dealing with supply chain processes and external compliance demands.

In developing countries, the productivity gap between small and large firms tends to be much more pronounced than in industrialized countries. For example, in India enterprises with more than 200 employees have been found to be ten times more productive than enterprises with five to 49 employees.⁸

One of the ways of closing the productivity gap is through engagement in trade through internationalization: internationally active firms tend to pay higher wages, employ more people and have higher productivity levels.

International trade continues to be dominated by large firms, which are better able to cope with market conditions as well as market power. Larger firms equally have the ability to invest in costly advisory services for analysis and compliance, as well as in technology tools to manage supply chains (such as supplier relations tools), and automate (part of) their trade compliance processes, such as

through applications (e.g. SAP Global Trade System, MIC or Amber Road trade compliance tools). Well-paid and relatively higher educated employees govern and coordinate complex supply chain processes. MSMEs on the other hand, rely on information provided by trade support institutions (TSIs) and sometimes (subsidized) advisory support.

Looking at the policy- and business environment related challenges, it can be said that small firms are adversely affected by tax, trade and access to finance policies, limiting their ability to fully harvest benefits from the open and rule-based trading system. In sum, the challenges include: lack of transparency and access to information; high trade costs resulting from Non-Tariff Measure such as standards and certification requirements; limited access to finance, and others.

Opportunities

As found by the WTO World Trade Report of 2018, new technologies may help reduce trade costs of MSMEs in developing countries and LDCs as well as developed countries, most notably by decreasing the relevance of distance, matching consumer preferences to products and facilitating searches. Looking at the specific opportunity of **e-commerce**, innovations such as cross-border payment systems offer MSMEs in developing countries and LDCs new opportunities to reduce trade costs.

Whereas the potential of new technologies to facilitate trade for MSMEs and developing countries disproportionately can be large, how exactly the changing trade environment should translate to new trade rules that are supportive for MSMEs

⁸ ITC MSME Competitiveness Outlook 2015, p. 4

development is yet to be fully understood.

Within the context of the WTO (and other international fora such as ICC), e-commerce is an area gaining substantial interest when looking at the interests of MSME's. Whereas rule-making in a WTO context is not supported by all WTO members (especially developing countries and LDCs wishing to keep to the agreed undertaking under the DDA), e-commerce has also been discussed in the context of the IWG on MSMEs (most notably the *de minimis* matter).

Conclusion

There are a number of proposals that have been put forward to enable MSMEs integrate in the multilateral trading system, be it through governance and coordination processes, enhanced rule-making, or considering assistance and support – especially targeting developing countries and LDCs.⁹ These will form the basis of the discussions in the IWG on MSMEs in the WTO that will be centred around the themes of (1) transparency and data availability, (2) coordination and outreach, and (3) special and differential treatment (SDT), technical assistance and capacity building

The growing attention for MSMEs in the context of WTO reflects increasing interest to deliver on inclusive growth and development. As WTO members continue reflections and discussions on WTO reform, and the need to update the WTO to meet 21st century realities, a window of opportunity exists to put forward proposals concerning the renewal and updating of visions on the underlying principles of the WTO (such as inclusiveness and transparency). Whereas the outcomes of WTO

reform discussions remain highly uncertain, the discussions around inclusiveness of the multilateral trading system may equally support concrete outcomes that enhance the role of MSMEs in international trade.

⁹ See the study on “Enhancing the participation of MSMEs in international Trade”



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