

**STRATEGIC CAPABILITIES AND EXPORT  
PERFORMANCE OF MANUFACTURING SMEs  
IN MALAYSIA: THE IMPACTS OF INDIVIDUAL,  
FIRM AND INDUSTRY LEVEL FACTORS**

by

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**Thesis submitted in fulfillment of the requirements  
for the degree of  
Doctor of Philosophy**

**September 2018**

## **ACKNOWLEDGEMENT**

First and foremost, my sincere appreciation and gratitude is extended to my supervisor, Professor Dr. Noor Hazlina Ahmad for her patience, dedication, comments, guidance and encouragement throughout this journey. I regard her as a very understanding and caring supervisor. Her confidence and belief in my capabilities have helped me improve tremendously as a scholar and researcher.

My sincere thanks also go to my co-supervisor, Associate Professor Dr. Hasliza Abdul Halim for her advice and support that given to me. I would like to acknowledge Professor T. Ramayah from School of Management, USM, Dr. Jacky Cheah from faculty of Economics and Management, UPM and Dr. Francis Chuah from School of Business Management, UUM for providing invaluable and priceless insights on the data analysis using Partial Least Squares (PLS) methods for this thesis.

My appreciation also goes to my husband and children who understand and as a backbone that encourage me to complete my study. Their prayers, encouragement and unconditional love inspired me to be a strong person in completing my study. Last but not least, to my best friends Nora, Najihah, Melissa whom I share the laughter and tears during good and tough times and always lending a helping hand when it is most needed, thank you very much.

## **TABLE OF CONTENTS**

<b>ACKNOWLEDGEMENT</b>	ii
<b>TABLE OF CONTENTS</b>	iii
<b>LIST OF TABLES</b>	viii
<b>LIST OF FIGURES</b>	x
<b>ABSTRAK</b>	xi
<b>ABSTRACT</b>	xiii
 <b>CHAPTER 1- INTRODUCTION</b>	
1.1 Introduction	1
1.2 Research Background	6
1.2.1 Business Internationalisation of SMEs	6
1.2.2 Relevance of Manufacturing SME to National Economy	8
1.2.3 Export Performance of Manufacturing SMEs	10
1.2.4 The Importance of Strategic Capabilities to SMEs	11
1.2.5 Government Export Assistance to SMEs	12
1.3 Problem Statement	16
1.4 Research Objectives	23
1.5 Research Questions	24
1.6 Scope of Study	24
1.7 Significance of Study	25
1.7.1 Theoretical Contribution	25
1.7.2 Practical Significance	29
1.8 Organisation of Thesis	32
1.9 Operationalisation of Key Terms	32
1.10 Conclusion	36
 <b>CHAPTER 2 - LITERATURE REVIEW</b>	
2.1 Introduction	38
2.2 Overview of SMEs and Internalisation of SMEs in Malaysia	40
2.3 Underpinning Theories of Export Performance	43
2.3.1 Resource-Based View (RBV) Theory	43
2.3.2 Dynamic Capability Theory	45

2.3.3	Internationalisation Theory	48
2.3.4	Linking Theories and Key Constructs	50
2.4	Export Performance	52
2.5	Strategic Capabilities	56
2.5.1	Innovation Capability	60
2.5.2	Marketing Capability	64
2.5.3	Market-Linking Capability	67
2.5.4	Technology Capability	68
2.5.5	Management Capability	70
2.6	Empirical Studies Links Strategic Capabilities and Export Performance	72
2.7	The Antecedents of Strategic Capabilities	72
2.7.1	Individual-Level Factors	72
2.7.1(a)	Export-Market Orientation	73
2.7.1(b)	Empirical Studies Links between EMO and Export Performance	77
2.7.2	Firm-Level Factors	81
2.7.2(a)	Human Capital	81
2.7.2(b)	Social Capital	83
2.7.2(c)	Organisational Capital	85
2.7.3	Industry Level Factors	87
2.7.3(a)	Technology Conditions	88
2.7.3(b)	Market Conditions	89
2.7.3(c)	Competitive Conditions	90
2.8	The Moderator: Government Export Assistance	91
2.9	Literature Gap	93
2.10	Theoretical Framework	94
2.11	Hypotheses Development	97
2.11.1	Links between Export Market Orientation and Strategic Capabilities	97
2.11.2	Links between Firm Level Factors and Strategic Capabilities	99
2.11.3	Links between Industry Level Factors and Strategic Capabilities	100
2.11.4	Links between Strategic Capabilities and Export Performance	102
2.11.5	Perceived Government Export Assistance as a moderator between Strategic Capabilities and Export Performance	103
2.12	Conclusion	104

## **CHAPTER 3 - RESEARCH METHODOLOGY**

3.1	Introduction	106
3.2	Research Design	107
3.3	Population and Sample	107
3.3.1	Population	107
3.3.2	Sampling Frame	109
3.3.3	Sampling Unit	110
3.3.4	Sample Size	111
3.4	Data Collection Procedure	111
3.4.1	Sampling Technique	112
3.5	Survey Instrument	113
3.5.1	Questionnaire Design	113
3.5.2	Pre-testing of Questionnaire	120
3.5.3	Data Preparation	121
3.5.4	Response Bias and Method Bias	122
3.6	Procedure for Data Analysis	123
3.6.1	Descriptive Statistics	123
3.6.2	Overview of Structural Equation Modelling (SEM)	124
3.6.3	Justification for PLS-SEM	125
3.6.4	Assessing Data Using PLS-SEM	128
3.6.4(a)	Assessment of the Measurement (Outer) Model	128
3.6.4(a)(i)	The Measurement Model for Reflective Construct: Reliability	129
3.6.4(a)(ii)	The Measurement Model for Reflective Construct: Validity	130
3.6.4(a)(iii)	The Measurement Model for Formative Indicators	131
3.6.4(b)	Assessment of the Structural (Inner) Model	133
3.6.4(c)	Analysis for Moderating Variable	136
3.7	Conclusion	137

## **CHAPTER 4 – DATA ANALYSIS**

4.1	Introduction	138
4.2	Data Collection	138

4.3	Data Screening	140
4.4	Respondents' Profile and Firm Information	140
4.5	Independent Sample T-Test and Common Method Variance	145
4.6	Goodness of Measurement	146
4.7	Assessment of Measurement Model	146
4.7.1	Assessment of Reflective Measurement Model	146
4.7.1(a)	Convergent Validity for Reflective Measurement Model	150
4.7.1(b)	Discriminant Validity for Reflective Measurement Model	152
4.7.2	Assessment of Formative Measurement Model	156
4.7.2(a)	Convergent Validity for Formative Measurement Model	158
4.7.2(b)	Collinearity Issues for Reflective Measurement Model	158
4.7.2(c)	Significance and Relevance of Outer Weight	161
4.7.3	Assessment for the Structural Model	162
4.7.3(a)	Assess Structural Model for Collinearity Issues	163
4.7.3(b)	Significance and Relevancy Assessment	164
4.7.3(c)	Level of $R^2$ (Coefficient of Determination)	168
4.7.3(d)	The Effect Size of $R^2$	172
4.7.3(e)	Predictive Relevance of the Model ( $Q^2$ )	174
4.7.3(f)	The Effect Size ( $q^2$ )	175
4.7.3(g)	Assessment of Moderating Variable	176
4.8	Summary of Hypotheses Testing Results	178

## **CHAPTER 5 – DISCUSSION AND CONCLUSION**

5.1	Introduction	183
5.2	Summary of Findings	183
5.3	Discussion on Antecedents of Strategic Capabilities	187
5.3.1	The Impact of Individual-Level Factor on Strategic Capabilities	187
5.3.2	The Impact of Firm-Level Factors on Strategic Capabilities	191
5.3.3	The Impact of Industry-Level Factors on Strategic Capabilities	199
5.4	Discussion on Direct Relationship between Strategic Capabilities and Export Performance	209
5.4.1	Innovation Capability and Export Performance	209
5.4.2	Technology Capability and Export Performance	211
5.4.3	Market-Linking Capability and Export Performance	213

5.4.4	Marketing Capability and Export Performance	216
5.4.5	Management Capability and Export Performance	218
5.5	Discussion on Government Export Assistance as Moderator between Strategic Capabilities and Export Performance	220
5.6	Theoretical Contribution	222
5.7	Practical Implications	225
5.8	Limitations	228
5.9	Directions for Future Research	230
5.10	Conclusion	231
	<b>REFERENCES</b>	234
	<b>APPENDICES</b>	

## **LIST OF TABLES**

		Page
Table 1.1	Number of Establishments by Sector and Size	8
Table 1.2	SME GDP Growth by Key Economic Activity (%) (Constant 2010 prices)	10
Table 1.3	Percentage Share of SME in Total Exports in Selected ASEAN (2000-2013)	17
Table 2.1	Definition of SMEs in Malaysia	41
Table 2.2	Summary on Export Performance Studies	52
Table 2.3	Empirical Studies Link EMO and Export Performance	79
Table 3.1	Distribution of SMEs in Manufacturing by Sub-Sectors	108
Table 3.2	Data Collection Procedure	112
Table 3.3	Key Constructs, Sources of Questions and the Number of Items	118
Table 3.4	Rules of Thumb for Selecting PLS-SEM or CB-SEM	125
Table 3.5	Measurement Model for Reflective and Formative Construct	133
Table 3.6	Measurement Criteria for Structural (Inner) Model	135
Table 4.1	Summary Table of Data Collection	139
Table 4.2	Summary Table of Respondents' Profile	141
Table 4.3	Summary Table of Firm's Background Information	142
Table 4.4	Summary of Reflective Measurement Model	150
Table 4.5	Discriminant Validity Using Fornell and Larcker Criterion	153
Table 4.6	HTMT Criteria Result	155
Table 4.7	Summary of Formative Model	162
Table 4.8	Path and Hypothesis Testing for Direct Impact of Antecedents	165
Table 4.9	Path and Hypothesis Testing for Direct Relationship	167



Table 4.10	Summary of Coefficient of Determination ( $R^2$ )	168
Table 4.11	Summary of The Effect Size ( $f^2$ )	173
Table 4.12	Summary of Predictive Relevance ( $Q^2$ )	175
Table 4.13	Summary of The Effect Size ( $q^2$ )	175
Table 4.14	Path Coefficient and Hypothesis Testing of Moderator	177
Table 4.15	Summary of Hypotheses Results	179

## LIST OF FIGURES

		<b>Page</b>
Figure 1.1	Manufacturing Export by Products	4
Figure 1.2	Components of SMEs in Manufacturing Sector (%)	9
Figure 2.1	Contribution SMEs to GDP at Constant 2010 Prices year 2017	42
Figure 2.2	Lin and Wu (2014) Conceptual Framework of RBV	50
Figure 2.3	Raymond and Pierre (2010) Research Framework on Internationalisation of Manufacturing SME	51
Figure 2.4	Theoretical Framework	96
Figure 4.1	Model Framework	148
Figure 4.2	Redundancy Analysis for Convergent Validity of Formative Model	160

**KEUPAYAAN STRATEGIK DAN PRESTASI EKSPORT PKS PEMBUATAN  
DI MALAYSIA: KESAN FAKTOR-FAKTOR INDIVIDU, FIRMA DAN  
INDUSTRI**

**ABSTRAK**

Kajian ke atas prestasi eksport dalam kalangan PKS di Malaysia menjadi signifikan pada hari ini apabila eksport menjadi sumber pendapatan utama negara. Ia sangat penting kepada PKS terutama negara yang sedang membangun seperti Malaysia untuk melihat dan membentuk keupayaan strategik mereka terhadap persaingan global dan peluang perniagaan demi meningkatkan prestasi eksport. Secara spesifik, kajian ini bertujuan untuk menentukan kesan faktor-faktor tahap individu, firma dan industri terhadap keupayaan strategik dalam meningkatkan prestasi eksport. Selain meletakkan keupayaan strategik sebagai penentu prestasi eksport, kajian ini juga menguji peranan bantuan eksport daripada kerajaan samada ianya menguatkan lagi perhubungan diantara keupayaan strategik dan prestasi eksport. Rangka kajian ini dibentuk berdasarkan kombinasi Teori Pandangan Asas-Sumber (*Resource-Based View Theory*), Teori Keupayaan Dinamik (*Dynamic Capability Theory*) dan Teori Pengantarabangsaan (*Internationalization Theory*). Kaedah kuantitatif digunakan dalam kajian ini dan sebanyak 187 maklumbalas daripada pengeksport PKS dianalisa menggunakan teknik Partial Least Squares (PLS). Keputusan menunjukkan bahawa Orientasi Pasaran Eksport (*Export-Market Orientation*) tidak memberi kesan signifikan terhadap keupayaan strategik, manakala, sebahagian daripada modal intelek dan keadaan persekitaran memberi kesan positif dan signifikan terhadap keupayaan strategik mereka. Keupayaan strategik dari segi inovasi dan teknologi memberi kesan signifikan terhadap prestasi eksport dan bantuan

eksport kerajaan dalam bentuk kewangan menguatkan perhubungan diantara keupayaan strategik (keupayaan pemasaran dan keupayaan inovasi) dan prestasi eksport. Hasil kajian ini juga memberi implikasi yang bernilai dari segi teori dan praktis.

**STRATEGIC CAPABILITIES AND EXPORT PERFORMANCE OF  
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**ABSTRACT**

Research on export performance among SMEs in Malaysia has become more significant nowadays as export is a major source of income for most countries. It is important for SMEs especially those in emerging countries like Malaysia to look into and put their efforts to strategize their capabilities to respond to the global competition and business opportunities in enhancing their export performance. Specifically, the study attempts to examine the impacts of individual level factor, firm level factors and industrial level factors towards strategic capabilities in enhancing the export performance. While considering strategic capabilities as having significant impact on export performance, this study also examines the role of government export assistance as moderator whether it strengthening the relationship between strategic capabilities and export performance. Drawing upon the combination of Resource-Based View Theory (RBV), Dynamic Capability Theory and Internationalization Theory, a conceptual framework is developed for further investigation. A quantitative approach was employed in this study and a total of 187 responses from SME exporters were received and further analyzed using Partial Least Squares (PLS) technique. The results demonstrated that; Export-Market Oriented (EMO) has no significant impact on strategic capabilities, while intellectual capital and environmental conditions partially have positive and significant impacts on some elements of strategic capabilities. Strategic capabilities in terms of innovation and technology have positive and significant impacts on export

performance and government export assistance in the form of access to financing strengthens the relationship between strategic capabilities (marketing capability and innovation capability) and export performance. The findings also provide invaluable implications to both theory and practice.

## **CHAPTER 1**

### **INTRODUCTION**

#### **1.1 Introduction**

Malaysian SMEs' export performance has continuously become the focus of researchers, practitioners and policy makers given the heightened awareness of the significance of exports as a major source of national income. In the Malaysian context, these developments are intensified by the ASEAN Economic Community (AEC) that strives to develop a stable, prosperous, highly competitive and economically integrated market and production base that can expedite trade and investment (MITI, 2015). AEC make to the markets in ASEAN region becoming a single market, globally diffuse source of invention (Muangkhrot & Ussahawanitchakit, 2015); manufacturing capability and innovation (Teece, 2007) as firms depending on their resources to drive to be more competitive.

The establishment of the AEC in 2015 is a major milestone in the regional economic integration agenda in ASEAN, offering opportunities in the form of a huge market of US\$2.6 trillion and over 622 million people. In 2014, AEC was collectively the third largest economy in Asia and the seventh largest in the world. In this sense, Malaysia's exports have increased with total exports to ASEAN markets rising to RM230.93 billion in 2016 from RM 213.40 billion in 2014 (Star online, 11 July 2017). AEC is seen as an important initiative as Malaysia seeks to expand market access opportunities, enhance competitive advantage, build investor confidence, draw foreign investments and build

capacity through Foreign Trade Agreements (FTAs). The varied opportunities offered by this agenda have somewhat forced Malaysian SMEs to develop their resources and enhance capabilities, so that they can compete globally and remain as major contributors to the national income.

Notably, the opportunities afforded in this era of globalization are vehicles for firms to expand their businesses internationally. In embracing this globalization agenda, SMEs are expected to be more aggressive and competitive to venture beyond their backyard and into the international markets. According to Senik, Isa and Ayob (2014), and Ahmad (2014), given the dynamic global market conditions, Malaysian SMEs are urged to pursue growth in international markets and seek its economic benefits.

Exporting is seen as an important activity that can ensure growth, profitability and survival in the current dynamic business setting. Exporting is said to be the most cost-effective and less risky mode to penetrate international markets, often occurring at the initial stages of the internationalization process for SMEs (Jones, 2001). Regrettably however, despite various support mechanisms and stimulus packages offered to local SMEs, the export contribution of Malaysian SMEs is still considered low especially if compared to its neighbours such as Singapore, Indonesia, Vietnam, Philippines and Thailand (Tambunan et al., 2015). The study revealed that Thailand is the most export-oriented SMEs which contributed 30-40 percent of total SME manufacturing export, Vietnam (20-29%), Philippines (20-26%), Indonesia (20%), Singapore (16%) and Malaysia (15-19%) of total contribution on export performance.

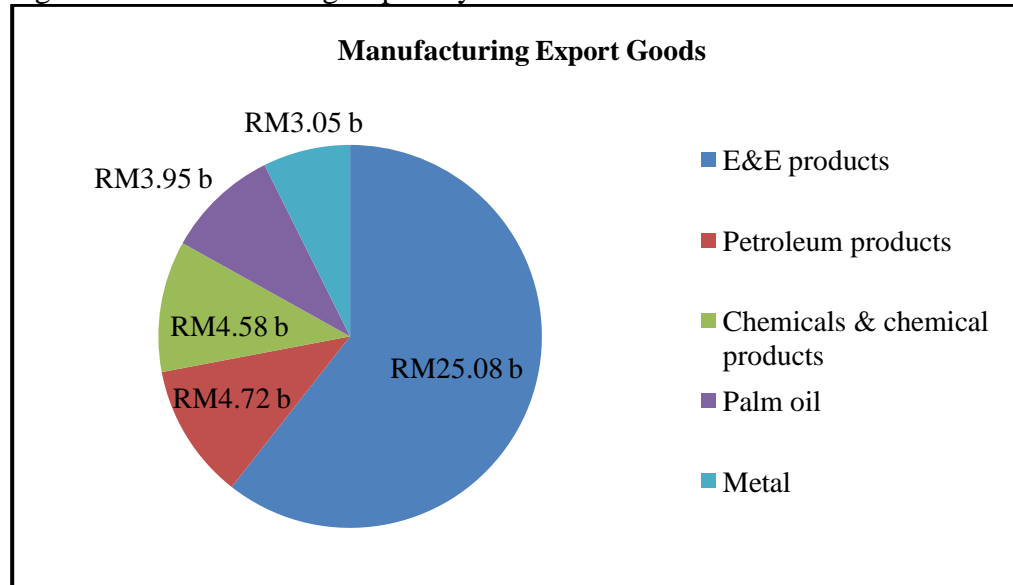


Many factors may explain this variety, such as government supports to exporting SMEs, infrastructure and logistic which have significant effects on transaction costs and hence regional price competitiveness of exporting SMEs, access to capital, technology, skilled manpower, raw materials and information, and, of course, not less important, level of 'internationalization' of entrepreneurs or owners of local SMEs (Tambunan et al., 2015). The total export of SMEs is only 18.6 percent which is markedly low than the goal to increase to 25 percent by 2020 (SME Annual Report 2016/2017).

The local SMEs have received remarkable support from the government to enable them to enter international markets. For instance, the Ministry of International Trade and Industry (MITI) assists the internationalization of SMEs by bringing them together via the ASEAN Economic Community (AEC). The AEC's role is to transform ASEAN into a region with free movement of goods, services investment, skilled labour, and a freer flow of capital (MITI, 2015). Such conditions will encourage the smaller firms to export their products worldwide.

Consequently, SMEs in the manufacturing sector have begun exporting their products and services to enhance performance. For example, Malaysia External Trade Statistics, (2015) reported that overall export for manufactured Electrical and Electronic (E&E) products stand at RM25.08 billion, petroleum products (RM4.72 billion), chemicals and chemical products (RM4.58 billion), palm oil which includes crude palm oil; palm kernel oil, oil and stearin (RM3.95 billion) and manufactures of metal (RM3.05 billion). This is depicted in Figure 1.1.

Figure 1.1 Manufacturing Export by Products



Source: Department of Statistics, Malaysia (2015)

Despite the strong potential to grow globally, the major challenges faced by Malaysian SMEs especially with regard to resource constraints, has somewhat slowed their internationalization process (Hashim, 2012). Some of the challenges faced by Malaysian SMEs include lack of human capital, lack of technology adoption (Hasnan et al., 2014), lack of skilled workers, poor infrastructure, ineffective implementation of government aids, lack of market and product knowledge, limited financial ability, less innovative and flexible, limited ICT involvement, increasing operational costs and failure to fulfil customer demand (Hashim, 2012).

The productivity and efficiency of these SMEs are also compromised due to the shortage of skilled workers in the labour market, resulting in the inability to upgrade the quality of their products for local and foreign markets. On that note, SMEs need to enhance their production capabilities to effectively respond to the fast-changing global market demands and enhance their export performance. While it is vital for SMEs to develop internal capabilities, the

role of government support in boosting their performance is also important and is seen as a conduit to scale up the export performance of SMEs. The GoEx high impact programme, for instance, was initiated by MATRADE to encourage export-ready SMEs to internationalize. Notably, RM129.5 million (5.2% of total allocation) has been provided to fund the programmes for SMEs to expand into new and export markets (SME Annual Report 2016/2017).

Other strategic efforts needed to respond to the internationalization agenda and global competition according to Parnell et al. (2015) include enhancing the companies' marketing, market-linking, technological, and management capabilities. Such strategic capabilities are claimed to enhance the export performance and allow subsequently sustain in the long run.

A scrutiny of the available literature emphasizes the knowledge gap about how SMEs capitalize their strengths to increase export performance, particularly those from newer economies. The limited literature focuses mostly on a specific level such as the firm level in terms of social capital (Khurram et al., 2014), distinctive capabilities (Man, 2009), innovation capability (Arumugam et al., 2013; Khurram et al., 2014), technological capability (Rasiah & Shan, 2015) and competitive capabilities (Ho, Ahmad, & Ramayah, 2016).

Given the lack of comprehensive framework that addresses SME export performance especially in the context of developing countries, this research seeks to build on prior research by integrating the individual-level, firm-level and industry-level factors as a holistic view to examine how each level accounts for the development of strategic capabilities that influences SME

export performance. Specifically, the study looks into how manufacturing SMEs capitalize their individual-level factors such as export market orientation (EMO) which is the employees' attitudes towards export information; firm-level factors related to the human, social and organizational capital of the firm; and industry-level factors involving the technology, market and competitive conditions that could enhance their capabilities. Also, the study examines the moderating role of government export assistance in strengthening the relationship between strategic capabilities and export performance.

## 1.2 Research Background

### 1.2.1 Business Internationalisation of SMEs

Internationalisation of SMEs includes all forms of transferring goods and services across borders (Ramonette et al., 2010). According to McGrath, (2013) it is imperative that smaller firms operating international businesses today develop their own capabilities and competitive advantage. Muhammad et al., (2010) noted that there is ample evidence to demonstrate that SMEs have realized the importance of international presence to sustain businesses. In Malaysia, SMEs are becoming increasingly active and rapidly expanding their businesses in international markets (Halim & Zain, 2011). Additionally, the SME Master Plan (2012-2015) clearly states that, "the role as enabler of growth will continue as SMEs upgrade from the current second-and third-tier suppliers to first-tier suppliers and link with large firms in the global supply chain". Thus, such opportunities for growth leads to greater income from increased export sales (MITI, 2015).

Accordingly, to reflect the structural changes in the nation's economy and recent economic developments including price inflation, structural changes, and changes in business, a new SME definition was introduced on 1st January 2014. The revised definition also concurs with the SME Annual Report, 2013/2014. Manufacturing SMEs refers to firms with sales turnover not exceeding RM50 million or full-time employees not exceeding 200 workers. Firms from service and other sectors are to have sales turnover not exceeding RM20 million or full-time employees not exceeding 75 workers (SME Corp, 2015).

The development and growth of SMEs in the international arena have substantially contributed to various economic benefits. For instance, the Department of Statistics, Malaysia (DOSM) (2017) reported that in Malaysia, SMEs accounted for 98.5 percent of the total establishment, contributed about 65.3 percent of employment and 36.6 percent of the GDP (SME Annual Report, 2016/2017). This illustrates the importance of SMEs in supporting and upholding the momentum of the Malaysian economy.

Ideal healthcare Sdn Bhd (IHSB), for instance, formerly known as Mutiara Medical, is one of Malaysia's leading providers of quality disposal medical and healthcare products. Through the GoEX program initiative, the company has been able to secure export sales contributing to some 25 percent of the company total sales in 2016. Similarly, CALMS Technology Sdn Bhd, a provider of leading edge solutions for multiple application Smartcards and Radio Frequency Identification (RFID), offers off-the-shelf solutions suitable for government, retail, education, enterprises and finance sector. The company

supplies services covering Card Issuance and Management System (CALMS-e), Visitor Management System (ViMS), Meal Redemption System (eMeRS) and Time Attendance Systems (TAMS). In October 2016, the company established negotiations with Mastech Co. Ltd. to provide ViMS to Myanmar.

### 1.2.2 Relevance of Manufacturing SME to National Economy

SMEs in the manufacturing sector are indispensable to the nation's economy. The Census Report on SMEs 2016 recorded a total of 920,624 companies in Malaysia and SMEs account for 907,065 of the total. Out of the total number of SMEs, 47,698 are from the manufacturing sector whilst 23,096 constitute for small and 2,519 for medium industries respectively as depicted in Table 1.1.

Table 1.1 Number of Establishments by Sector and Size

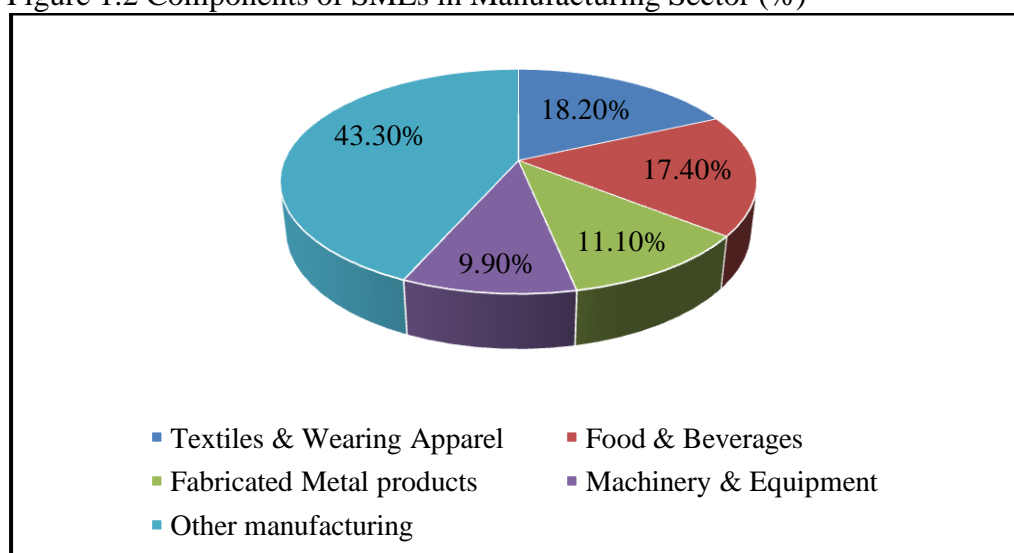
Sector	Micro	Small	Medium	Total SME	Total SME	Large Firms	Total
	Number of Establishments				% Share		
Manufacturing	22,083	23,096	2,519	47,698	5.3	1,403	49,101
Services	649,186	148,078	11,862	809,126	89.2	9185	818,311
Agriculture	4,863	4,143	1212	10,218	1.1	1,410	11,628
Construction	17,321	17,008	4,829	39,158	4.3	1,400	40,558
Mining & Quarrying	217	458	190	865	0.1	161	1026
<b>Total</b>	<b>693,670</b>	<b>192,783</b>	<b>20,612</b>	<b>907,065</b>	<b>100</b>	<b>13,559</b>	<b>920,624</b>

*Source: Profile of Small and Medium Enterprises (reference year 2016), Department of Statistics, Malaysia*

Yet despite their large composition, SMEs contributed to only 18.6 percent of the total export performance in 2016 (SME Annual Report 2016/2017). Out of this, 9.4 percent was from services sector, 8.8 percent points was derived from manufacturing and the remaining from agriculture. In

the manufacturing sector, most SMEs are concentrated in the textiles and apparel, food and beverages (F&B) products, fabricated metal products as well as machinery and equipment sub-sectors. Other manufacturing sectors include printing, producing furniture, rubber and plastic products, wood products, electrical and electronics (E&E). The component distribution is depicted in Figure 1.2 as reported by the Department of Statistic, Malaysia, 2017.

Figure 1.2 Components of SMEs in Manufacturing Sector (%)



Source: Department of Statistics, Malaysia (2017)

Various benefits are related to exporting, such as market opportunities, increased profit, business expansion (Halim & Zain, 2011) and better use of production technology (Le & Valadkhani, 2014). In general, exporting is also considered to be the primary and most popular method (Halim & Zain, 2011) used by small business in their internationalization process. The manufacturing SMEs mostly choose to expand their business via exports (Ahmad, 2014).

Nonetheless, despite the potential cumulative contribution of SMEs to the country's economy, the involvement of Malaysian SMEs in the international market remains small (Khan & Khalique, 2014). The manufacturing SMEs are seen struggling to generate income via international

markets and exports (SME Corp, 2014). This does not resonate with the latest SME annual report (MITI, 2015) that the manufacturing sector is expected to be led by export-oriented industries in line with increased external demand. Additionally, exporting has its own challenges especially to SMEs as they lack resources and capabilities compared to larger firms (Rosnan et al., 2016).

### 1.2.3 Export Performance of Manufacturing SMEs

The performance of manufacturing SMEs does not appear to be very encouraging given the drop in their GDP growth contributions (as shown in Table 1.2). The manufacturing SME GDP contribution for 2016 is recorded at 4.8 percent, illustrating a tremendous reduction from 10.8 percent in 2014. The total SME GDP also decreased from 13.5 percent in 2014 to 5.2 percent in 2016 despite exports of SMEs increased by 6.6% in 2016, rebounded from 0.1% decline in 2015 (SME Annual Report, 2016/2017).

Table 1.2 SME GDP Growth by Key Economic Activity (%) (Constant 2010 Prices)

Year	2014	2015	2016
Agriculture	17.3	2.0	-1.7
Mining & Quarrying	183	8.9	8.2
Construction	97.6	7.6	6.8
Manufacturing	10.8	6.0	4.8
Services	2.6	7.0	6.9
Plus: import duties	21.6	20.3	9.9
<b>Total SME GDP</b>	<b>13.5</b>	<b>6.1</b>	<b>5.2</b>

Source: Department of Statistics, Malaysia (2017)

Additionally, the export contribution of Malaysian SMEs is still low despite their huge numbers (907,000) (The Sun, April 2017). In his speech to BERNAMA at the Beyond Nations Public Contest prize ceremony, 20<sup>th</sup> April 2017, the MATRADE CEO, Dr. Mohd Shahreen Zainooreen Mad Ros emphasised “the crucial role of SMEs to the economy and social development as they contribute nearly 36 percent of the country’s GDP and 65 percent of the



country's employment". Moreover, there are abundant opportunities overseas for Malaysian companies to tap into, with ASEAN countries and other countries such as United States of America (USA), Latin America, Europe and Africa. Currently, Malaysian SMEs have a market population of 1.4 billion people from China (Malaysia's biggest trading partner) and 1.3 billion people from India (Malaysia's emerging trading partner) (MATRADE, 2017). As such, the launch of the ASEAN Economic Community (AEC) is set to open up business opportunities from its single market especially to SMEs. The ability to grow businesses, participate and network internationally provides credence to SME capabilities. Such capabilities ensure that these SMEs can face stiff competition as a result of recent developments in the Asian commercial landscape.

#### 1.2.4 The Importance of Strategic Capabilities to SMEs

In order to survive and thrive in a competitive business environment, all businesses especially, the smaller firms, need to possess specific strategic capabilities (Johannesson & Palona, 2010) with regard to innovation, marketing and technologies that support the global growth of manufacturing SMEs (Raymond et al., 2014). Such capabilities can be leveraged if firms take persistent efforts and strategize to increase their export performance.

Prior research defines capabilities mostly as resources that are unique to the organization that places it above its competitors. Madhok (1998) defines the capabilities as a combination of resources that creates higher-order competencies. Moreover, capabilities are complementary when the returns to one capability are affected by the presence of another (Brynjolfsson &

Milgrom, 2012). Additionally, Morgan et al., (2012a) noted that the interconnectedness of the capabilities creates causal ambiguity that makes it difficult for competitors to identify the source of a firm's observed performance advantage. Hence, such complementary capabilities can increase the firm's effectiveness and limit rivals' ability to successfully imitate the resources of others.

In the Malaysian context, previous studies on strategic capabilities are still limited and focus only on technological capabilities (i.e. Rasiah & Shan, 2015), innovative capabilities (i.e. Alam et al., 2011; Khurram et al., 2014; Rosli, 2012), distinctive capabilities (i.e. Man, 2009) and competitive capabilities (i.e. Ho et al., 2016). Hence, there is a call to look into SME capabilities to understand how their performance and competitiveness can be enhanced. This study therefore examines the relationships of strategic capabilities that comprise innovative, market-linking, marketing, technology and management capabilities with the export performance of Malaysian Manufacturing SMEs. It is also conjectured that government support towards SMEs enhances the relationship between strategic capabilities and export performance.

#### 1.2.5 Government Export Assistance to SMEs

It is well acknowledged that SMEs have limitations in terms of finance, capital, skills and capabilities and industrial experience if compared to larger firms (Hashim, 2015). In view of this handicap, the Malaysian government continues to provide support to encourage Malaysian SMEs to spread their wings to the global arena with varying export assistance initiatives. Starting

from the establishment of National SME Development Council (NSDC) in 2004, the Government has implemented various SME development programs through its ministries and agencies.

The SME Annual Report 2016/2017 highlighted that a total of 148 SME development programs has been implemented by the Government in 2017 with a financial commitment of almost RM250 billion for the benefit of 66,410 SMEs. Besides, the Government through its ministries and agencies in collaboration with the private sector is conducting 21 programs with a financial commitment of RM3.34 billion mainly to assist 14,450 SMEs. Altogether, there were 169 SME development programs being implemented in 2017 with a financial commitment totaling RM5.85 billion for 80,860 SME beneficiaries (SME Annual Report 2016/2017).

The programs addressed key factor areas, namely access to financing, innovation and technology adoption, human capital development, market access, infrastructure as well as legal and regularity environment (SME Annual Report 2016/2017). Majority of these programs endeavour to raise SME productivity and competitive edge, considered the most important goals of the SME Master Plan. The government allocated RM1.93 billion for access to financing programs, RM236.7 million for innovation and technology adoption, RM137.7 million for human capital development, RM129.5 million for market access, RM61.7 million for infrastructure and RM8 million for SME on Legal and Regulatory Environment to assist SMEs in navigating the regulatory aspects and ease the regulatory burden for the entrepreneurs.

Exclusively, the government implemented the ‘Going Export’ (GoEx) program purposely for SME exporters as one of the High Impact Programs (HIP) of the SME Master plan. The Malaysia External Trade Development Corporation (MATRADE) was appointed as the implementing agency of the program to nurture local SMEs to become more resilient and competitive in the international marketplace (SME Corp., 2017).

In relation to the GoEx program, the Ministry of International Trade and Industry (MITI), through SME Corporation Malaysia (SME Corp. Malaysia), has implemented the SME-Brand Development Program. This program aims to create awareness on branding among SME through seminars, workshops and advisory services via Branding Innovation Centre (BIC) and Branding and Packaging Mobile Gallery. SME Corp. reported that a total of 270 SMEs benefited from this program with an expenditure totaling RM2.4 million (MITI, 2015). Likewise, a National Mark of Malaysia Brand, a certification process audited and monitored by SIRIM, was also introduced as part of its effort to encourage SMEs to go global. The Malaysian Brand is developed not just for the local market but with the intention that they would be good enough too to penetrate international markets (SME Annual Report, 2016/2017).

To support the brand SME-Brand Development program, MATRADE has also planned 147 trade promotion activities since 2014. These comprise of the SMEs participation in International Trade Fairs, Specialized Marketing Missions (SMM), In-coming Buying Missions, Joint Promotion Activities and organization of three major international exhibitions; Malaysia International

Halal Showcase (MIHAS), Malaysia Services Exhibition (MSE) and International Trade Malaysia (INTRADE) (MATRADE, 2014). In essence, they represent a branding initiative to enhance the visibility of Malaysian products and services in both local and international markets (SME Annual Report 2016/2017). For the exporters' development, MATRADE programs will focus on grooming and strengthening the competitiveness of Malaysian exporters, especially the SMEs, by providing focused training based on the companies' state of export readiness, market orientation and industry sectors (MATRADE 2017).

Besides, other High Impact Programs planned by the government to assist SMEs include the Technology Commercialization Platform that was implemented by the Ministry of Science, Technology and Innovation (MOSTI) to promote innovative ideas, the concept of commercialization, provide linkages and other related information. In relation to the program, the long-term Pre-Commercialization Fund was implemented by the ministry (MOSTI) to assist entrepreneurs in developing processes, technologies, or new products and improvements to be commercialized (MITI, 2015). Such assistance programs hope to assist in increasing export performance in the future.

At the same time, efforts persist in developing human capital through high quality training such as the Coach & Grow Program designed to provide entrepreneurs with the tools and know-how to implement strategies during the commercialization and growth stages. Other training initiatives include the Entrepreneurship Development Programs which focus on enhancing technical knowledge and skills of existing, potential and new entrepreneurs. Under this

training, the participants are equipped with information on business opportunities, financial assistance and loans, infrastructure facilities and the latest programs. The Ministry of Human Resources (MOHR) has also allocated RM14.5 million for its HR Capabilities Building Program for SMEs. These training-oriented programs are designed to equip entrepreneurs and their workforce with the knowledge, skills and qualifications to boost productivity, increase quality of service, encourage business expansion and improve individual capabilities (MITI, 2015). The programs benefit their preparation to serve and manage their business operations in international markets.

Despite the abundant support mechanisms offered by the government, the growth of SME export performance does not seem satisfactory. Hence, the present study attempts to examine the factors that enhance export performance among homegrown SMEs. The study also examines the extent to which the government assistance programs strengthen SME capabilities, thus subsequently enhancing export performance.

### 1.3 Problem Statement

It is well noted that SMEs are significant to Malaysia's economic development. The SME sector contributed about 35.9 percent to the Gross Domestic Product in 2015, accounting for 19 percent of exports (SME Corp, 2016). The Malaysian government offered extensive support by providing SME development programs through its agencies such as MATRADE, MOSTI, MOHR to help SMEs compete and recognize opportunities in market access provided by changes in the global landscape, as elaborated in section 1.2.5.

Unfortunately, the export performance of SMEs in Malaysia is among the lowest (between 15-19 percent) if compared to their neighbouring counterparts. Table 1.3 illustrates current estimates of SME contributions to total national exports in selected ASEAN countries, 2000-2013, as depicted in a recent study by Tambunan et al., (2015).

Table 1.3 Percentage Share of SME in Total Exports in Selected ASEAN (2000-2013)

<b>Country</b>	<b>Average Share (%)</b>
Thailand	30-40
Philippines	20-25
Vietnam	20-29
Indonesia	16
Singapore	16
Malaysia	15-19

*Source: Adopted from Tambunan et al., (2015)*

Furthermore, MITI (2015) reported that for the period of January-May 2015, trade with ASEAN was valued at RM155.99 billion, accounting for 27.2 percent of Malaysia's trade, with exports of RM85.43 billion and imports at RM70.56 billion. Recently however, the Malaysian export to ASEAN countries demonstrated a descending trend from 2013 to 2014, for instance export to Singapore decreased by 4.8%, Indonesia (16%), Philippines (5.8%), Myanmar (10.9%), Brunei (15.1%) and Laos (40.9%) consecutively (MITI, 2015).

It is reported that small and medium enterprises (SMEs) in the manufacturing sector contribute significantly to the economic growth of the country (Ho et al., 2016). Notwithstanding this, the performance of manufacturing SMEs appears to be waning given the drop in the GDP growth contributed by the manufacturing SMEs as previously mentioned in section 1.2.3. The manufacturing SME GDP growth was recorded at 4.8 percent in 2016, a tremendous reduction from 10.8 per cent in 2014.

As Malaysia is ranked among the lowest exporters in comparison to other neighboring countries, coupled with their decreasing export performance trend as reported by MITI 2015, action needs to be taken should Malaysian SMEs wish to achieve the objectives stipulated in the SME Master Plan. It is recognized that one of the challenging issues that affects the manufacturing sector is lack of capabilities such as innovation, technology support, talent or human skills, access to market and finance (RMK 11, 2015). Moreover, SMEs also face other key constraints in terms of business networks, lack of managerial skills and also lack of marketing capabilities (Jamak et al., 2014). Procedures and regulations also disproportionately affect SMEs compared to large firms (MITI, 2017).

In addition, a previous report by Muhammad et al., (2010) noted that the lack of managerial capabilities in a globalized environment hampered SMEs in their export performance. Thus, businesses need to continuously search for new opportunities for growth, enhance their capabilities, acquire new skills, adopt unconventional solutions, and consider changes in mindsets and attitudes towards work to be more competitive (MITI, 2015).

Similarly, Sin (2010) mentioned that SMEs in Malaysia are still facing problems such as limited capabilities in meeting the challenges of market liberalization and globalization, limited capacity for technology management and knowledge acquisition, shortage of skills for the new business environment and low productivity and quality output. Unfortunately, also, the 2011 Global Entrepreneurship Monitor (GEM) report published by the World Bank indicated that Malaysia compares less favorably vis-à-vis other countries due to



their perceived capability in entrepreneurship. Furthermore, the integration of the ASEAN economy through the ASEAN Economic Community (AEC) Blueprint, as adopted in 2007, compelled Malaysia to be more indomitable to succeed.

Zou et al., (1998) reported that most studies on the export performance of manufacturing SMEs have been conducted in developed countries. Despite the increased attention paid to this sector, not much has been researched on the SME export performance in developing countries (Singh & Mahmood, 2014b). In addition, the available studies relating to export performance in Malaysia are conducted in a piecemeal fashion, focusing on one aspect at a time i.e. management skills and venture performance (Sambasivan et al., 2009) as well as export-led growth strategies (Khalafalla & Webb, 2001). Hence, by employing a more holistic approach, the present study attempts to close the gap by integrating the three factors, namely individual level, firm level and industry level factors that influence SME strategic capabilities to enhance export performance.

A scrutiny of past literature showed a variety of variables that have been explored to determine their effects on firms' export performance (see for example; Boehe & Cruz, 2010; Cadogan, Sundqvist, Salminen, & Puumalainen, 2002; Styles, Patterson, & Ahmed, 2008). Notably, the incorporation of strategy as a firm's internal capability that leads to enhanced export performance is still scant (Singh & Mahmood, 2014). Specifically, research in the aspects of marketing, technology, market-linking and management to improve the prospects for performance is much lacking

(Parnell, 2011). Moreover, according to Parnell (2011), empirical research examining the influence of business strategy and capabilities on smaller firms' performance in emerging countries is limited. Therefore, more empirical research into the relationship between capabilities and performance across a wider range of industries is also warranted (DeSarbo et al., 2005).

As argued by Lin, Huang and Peng (2014), studies that dwell into the exporter's behavior is required, for instance, export market orientation (EMO) is one of factors or behavior that could influence export performance. EMO is particularly important in an international context, because foreign markets are far more complex than domestic ones, and this complexity increases demand for market intelligence, dissemination, and responsiveness. Manufacturing SMEs in Malaysia are still lacking on the aspect of intelligence and responsiveness (Sanuri et al., 2014). They lack of information on potential markets and customers (Burhanuddin et al., 2009), where the information gathered by SMEs are only focusing on customer needs, otherwise information from outside organization system such as competitors, technology, government regulation and other environmental forces are also important (Kohli & Jaworski, 1990; Mokhtar et al., 2014).

Moreover, taking into account the complexity and uncertainty of foreign markets, some researchers have called for the conceptualization of a specific export market orientation (EMO) (Pascucci et al., 2016). A review of the literature also suggests that a relatively number of empirical studies have expanded market orientation research to international business environment (Chi & Su, 2013) and to small and medium sized firm (SMEs) in particular

(Singh & Mahmood, 2013) and, the exact nature of the relationship between individual-level EMO behavior and strategic capabilities that lead to better performance is still underexplored.

Likewise, firm-level factors are considered important for as observed by Huang and Wu (2010) , there is relatively little empirical research that examines the relationship between intellectual capital which includes human, social and organizational capital (firm-level factors) and firm capabilities that leads to export performance. According to Khalique, et al., (2011), intellectual capital is a very important factor for the success of organisations to take competitive advantage. Ding and Lin (2010) asserted that, in a knowledge-based economy the intellectual capital is gradually replacing the physical assets in modern enterprises. It is indispensable for modern and high technology enterprises to pay full concentration not only in products innovation, marketing channels, market and services, but also improve in research and development through the improvement of intellectual capital.

Manufacturing SMEs identified various challenges facing SMEs in globalized environment which related to intellectual capital, which include lack expertise of human capital (Ngah & Ibrahim, 2012); lack of skills and talented workers (Bennett et al., (1998); poor in storing knowledge (structural capital) (Kuan & Aspinwall, 2003; Levy, 2003); lack access to formal business and social networks (Teoh & Chong (2008); lack of good contacts with local and international enterprises (Hashim & Wafa, 2002; Muhammad et al., 2010), and Alam et al., (2011) observed that SMEs in Malaysia have social barriers which are main obstacles to achieve the competitive advantage and consequently

many SMEs in Malaysia lose out in terms of opportunities to expand their business internationally.

In addition to the effects of environment factors, this study integrates industry factors such as technology, market and competitive conditions to be analyzed as antecedent factors. SMEs in turbulent environment need to adopt the best strategic approach to face challenge the situation at hand in order to succeed in foreign market (Kaynak & Kuan, 1993). Also, Samson and Mahmood (2012) capitalized that when there is high degree of turbulent environment there would be a higher risk and uncertainty and reinforcing high level of proactive approach would be needed in the strategic planning. The fast-changing global industries environment for example, forcing SMEs to improve their competitiveness by analyzing the technology conditions, market conditions and competitive conditions. According to Burhanuddin et al., (2009), it is important for the SMEs to identify the primary obstacles they face with regard to adopting new technology and acquisition and to create tools and policies designed to help them overcome these specific challenges. The challenges also come from market in which fast changes in customer taste and preferences and competition in term of products and price with other producers, such as from Indonesia, China, Thailand and India (Burhanuddin et al., 2009) forcing SMEs to be more aggressive in exploiting and plan their business strategies.

Based on the above consideration, this research intends to determine the individual, firm and industry level factors that are conjectured to impact the strategic capabilities of the firm which could subsequently enhance their export

performance.

#### 1.4 Research Objectives

Based on the preceding discussion, this study aims to examine the strategic capabilities and export performance of manufacturing SMEs. The study also hopes to explore the extent to which factors at the individual-level, firm-level and industry-level (antecedents) will energize and enhance strategic capabilities. It is also believed that government export assistance is an important resource (as a moderator) that supports the exporters in increasing their export performance, as the moderator is assumed to strengthen the relationship between capabilities and export performance.

Therefore, this study attempts to meet the following objectives:

- 1) To examine the influence of individual-level factors (i.e. Export-Market Orientation) (EMO) on strategic capabilities of manufacturing SMEs in Malaysia.
- 2) To examine the influence of the dimensions at the firm-level (i.e. human capital, social capital and organizational capital) on strategic capabilities of manufacturing SMEs in Malaysia.
- 3) To examine the influence of industry-level factors (i.e. technology, market and competitive condition) on strategic capabilities of manufacturing SMEs in Malaysia.
- 4) To investigate the effects of strategic capabilities (i.e. innovation capability, market-linking capability, marketing capability, technology capability and management capability) on the export performance of manufacturing SMEs in Malaysia.

- 5) To test the moderating effect of government export assistance programs on the relationship between strategic capabilities and export performance.

### 1.5 Research Questions

Based on the research objectives, this study seeks to answer the following research questions:

- 1) To what extent does EMO, which is an individual-level factor, impacts the development of strategic capabilities of manufacturing SMEs in Malaysia?
- 2) To what extent do the dimensions at the firm-level (i.e. human capital, social capital and organizational capital) impact the development of strategic capabilities of manufacturing SMEs in Malaysia?
- 3) To what extent do the dimensions at the industry-level (i.e. technology, market and competitive condition) impact the development strategic capabilities of manufacturing SMEs in Malaysia?
- 4) To what extent do the strategic capabilities (i.e. innovation capability, market-linking capability, marketing capability, technology capability and management capability) impact the manufacturing SMEs' export performance?
- 5) Does government export assistance usage moderate the relationship between manufacturing SMEs' strategic capabilities and export performance?

### 1.6 Scope of Study

The study focuses on an empirical examination of the holistic impact of individual-level factors (i.e., Export-Market Orientation), firm-level factors

(i.e., human capital, social capital and organizational capital) and industry-level factors (i.e., technology, market and competitive conditions) to strategic capabilities that enhance manufacturing SMEs' export performance. The strategic capabilities include innovation, market-linking, marketing, technology and management capabilities.

This research also examines the role of government export assistance programs as a moderator in strengthening the relationship between the firm's strategic capabilities and export performance. In sum, this study is motivated by the quest to answer the question "Do the individual, firm and industry-level factors affect SME strategic capabilities and enhance export performance?"

This study targets the manufacturing sector SMEs in Peninsular Malaysia as the subject. According to SME Corp (2016), manufacturing and manufacturing-related services SMEs are enterprises with sales turnover of less than RM50 million or less than 200 full-time employees. To obtain the study sample, the Federation Manufacturing Malaysia (FMM) directory was utilized, given that it contains updated data on manufacturing firms in Malaysia (Muhammad et al., 2010), including those that undertake exporting activities. The selection of the sample is based on the inclusionary criterion set for the study that includes manufacturing firms having less than 200 employees and involved in exporting activities.

## 1.7 Significance of Study

### 1.7.1 Theoretical Contributions

In terms of theoretical contribution, the study firstly contributes to the