Sustainable Development Strategy of SMEs After the Global Financial Crisis in China

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Abstract: After the influence of the global financial crisis, the paper analyses the small and medium-sized enterprises (SMEs) strategy of sustainable development in China from a view of the Resource-Based Theory. The paper considers that the SMEs in China still cannot obtain enough capital from outer financing institutions although the Chinese government announced Rmb 4,000bn in additional stimulus measures in 2008 to help rescue the territory from the steepest economic decline in more than two decades. Lacking of financial resources lends to the poor reputation, physical resources, human resources, technological resources and organizational resources, and then discusses the path of the SMEs’ sustainable development: changing SMEs Financial Status by Improving operating efficiency and financial transparence; streamlining organizational processes and business models; operating as sustainable suppliers in global supply chains.

Keywords: SMEs, Financial Crisis, Sustainable Development, The Resource-Based Theory, China

1 Introduction

Under the equal external environment, how to SMEs sustainable development is an important strategy problem in China. According to resource-based theory, a firm’s internal environment, in terms of its resources and capabilities, is more critical to the determination of strategic action than is the external environment. Each organization is a collection of unique resources and capabilities that provides the basis for it’s the primary source and strategy of its returns. Barney¹ divided a firm’s resources into physical capital resources (e.g., equipment), human capital resources (e.g., experience), and organizational resources (e.g., a firm’s formal structure). Hitt et al.² viewed a firm’s resources as the input for its business process, and divided them into tangible resources (e.g., financial resources) and intangible resources (e.g., patents). This study considered the SMEs resources are the foundation for firm profits and the major source of firm capabilities, and divided them into financial resources, reputation, physical resources, human resources, technological resources and organizational resources; and the financial resources are critical factor.

Sustainable enterprise resilience is the capacity for an enterprise to survive, adapt, and grow in the face of turbulent change, and creates multiple business opportunities through green technologies, reduction of raw material and energy use, and discovering innovative pathways for recovery and reuse of waste streams in place of virgin resources, and at the same time, to increase shareholder value without increasing material throughput³.

The strategy of a sustainable enterprise has been defined as the process of aligning an enterprise with the business environment to maintain a dynamic balance. By adding a sustainability lens within the framework of SME strategic planning, SME development seeks to balance resilience and growth so as to align the creation of abundance: economically, environmentally, and socially, and to conserve that value for future generations⁴. Integrating sustainability into their competitive strategy, and thereby obtaining greater profitability for SMEs through adoption of intentional sustainable strategies, can help them to optimize their rate of sustainable change.
2 The SMEs’ Importance and Global Financial Crisis’ Influence to SMEs

2.1 The SMEs’ importance in economy
Social and economically, SMEs are a strong base for the economy of any country. For instance, 99.8% and 90% of all companies are SMEs in the UK and Europe, respectively. The European Commission 2006 stated that SMEs in the industrial sector could fluctuate according to macroeconomic indicators like the GDP due to their high indices of investment and contribution to the growth in employment. Some sustainability indicators, for example the Spanish Central Directory of Companies showed that SMEs 12.79% exert their activity in the construction sector, while the National Statistics Institute showed that the number of houses built had increased from 302000 units in 1995 to 750000 in 2006. In Colombia, the Administrative Department of National Statistics stated that the building sector participates in 5.2% of the GDP and SMEs in 2004 contributed to a 96.4% of the industrial activities and that 63% of employment is generated for SMEs. SMEs account for about 90 per cent of employment in Korea, as well as defined as those with fewer than 250 workers, now account for 58.7 per cent of the employment and 51.1 per cent, or £890bn, of turnover in the UK in 2008.
At the same time, the rise in the private sector (most are SMEs) has been one of the most important and least remarked upon aspects of the country's spectacular growth over the past two decades in China. The numbers are hard to pin down, but a report published in 2008 concluded that the private sector now accounted for 70 per cent of China's GDP and employed 75 per cent of the workforce. However, the Sustainable development of SMEs is still a worldwide problem because their small scale, big risk, poor credit, difficulty of financing guarantee, the problem is not only outstanding but also very ubiquitous. Therefore, the exploration and innovation of the Sustainable development of SMEs have important meaning. This study focuses on the firm’s internal strengths and weaknesses relative to their external opportunities and threats and the owner’s decisions of how to achieve Sustainable development.

2.2 The global financial crisis’ influence to SMEs
The roots of the global financial crisis started in the US, and lenders' exposure to sub prime real estate. So, the financial crisis that started in 2007 is the most serious setback the world economy has experienced since the great depression. There are numerous factors that have contributed to the financial crisis. Of particular importance are global macroeconomic imbalances, poor risk management practices, and weak financial regulations and supervision. With the economic situation deteriorating, companies across the world had already reduced their discretionary spending. For example, construction spending and residential and business investment all fell in the UK, Euro zone and US in the past two years. But the economic crisis has provided China with an opportunity to assert its economic influence. The Chinese government announced Rmb 4,000bn ($590bn) in additional stimulus measures in 2008 to help rescue the territory from its steepest economic decline in more than two decades. The measures include a raft of tax exemptions, public service payment waivers and credit support for small and medium-sized enterprises. In fact, to win mandates on plum infrastructure projects such as public housing and transport, banks have relaxed standards. Banks advanced Rmb5, 840bn ($855bn) of new loans in the first five months in 2009, almost triple the amount a year earlier. Meanwhile, big corporate are awash in liquidity: Some are simply putting loans on deposit, or lending on to lesser credits denied bank finance. However, in the first quarter, direct lending to SMEs–the engine of any economy–accounted for less than 5 per cent of the total. So we must accept that challenges remained in funding SMEs. But for the more entrepreneurial SMEs, the most promising engine of China’s future industrial development is not its state sector, but its millions of nimble privately-owned companies. There is much evidence that they are more enterprising, productive and innovative than their larger rivals.

3 SMEs’ Strategy of Sustainable Development
It is becoming apparent that voluntary, incremental environmental improvements by individual companies will be inadequate to significantly offset the growth of the global economy, and that the rapid growth of China, India, and other Asian economies will likely exacerbate this problem. Sustainability strategies create many synergistic effects for SMEs working collaboratively, as well as systemic benefits for the commons. This paper discusses several different scenarios for SMEs to optimize and use sustainability to create competitive advantages rather than simply focusing on reducing unsustainability.

3.1 Streamlining organizational processes and business models
One hurdle for larger organizations to surmount is that while they usually have adequate human capital assets and other resources, they are often caught facing the challenges of disruptive change with inappropriate and ineffective organizational processes and business models. An organization’s capacity to meet the challenges of disruptive change is affected by its resources, processes, and values. Initially, organizational resources determine the firm’s capabilities. As the firm matures, organizational processes become well-defined, and once the firm’s business model becomes clearly defined, organizational values are articulated. These factors – resources, processes, and values – are the building blocks of the organization’s culture. Christensen and Overdorf argue that changing a company’s processes, business models, values, and ultimately its culture is difficult, if not impossible, for large, established companies; and yet, this is precisely what must happen in order for a firm to deal with disruptive innovations and major changes. Smaller organizations can leverage their capacities for entrepreneurial innovations and organizational change, thereby, learning to achieve advantages over larger organizations.

3.2 Expanding SMEs competitive advantages
A second hurdle is that while larger organizations may do well initially with technological developments, their capability to ameliorate competitive constraints insulates them so that they are likely to become weaker competitors over time, compared with smaller organizations that cannot escape the rigors of technology survival contests. When disruptive innovation and change are driven by competition contests, larger organizations tend to have significant survival and competitive advantages. However, when a larger organization succeeds in neutralizing the constraints of competition, the organization’s perceived invulnerability serves as insulation from critical sources of continuous organizational development. Hence, strategies that isolate organizations from competition may actually backfire, such that larger organizations become weaker competitors in the long run. These implications suggest that since smaller firms cannot effectively constrain competitive forces nor shield themselves from these external forces, the organizational development processes of smaller firms may also constitute a built-in engine for addressing the challenges of disruptive innovation and change.

3.3 Changing SMEs financial status
In the process of SMEs proceeding to maturity, it is very common that they would encounter some a certain kind of financing gaps; that is, the demand of capital would exceed the supply of capital. According to the difference of financing channel, method and time limitation, enterprise financing can be divided into many types. In this paper, it is divided into inner financing and outer financing according to the resource-based theory. Inner financing is the capital raised from the enterprise interior including self-owned capital, depreciation and reserved income. Outer financing is the capital raised from the outside of the enterprise. It often includes bank loan, commercial financing (mainly credit purchase and promissory note), leasing financing, securities financing (mainly stock and bond financing), fiscal financing and international financing.

We notice that accounts payable is mainly come from trade creditors. Accounts payable accounts for the great percentage in the total liabilities of SMEs in different development phase. The SMEs in creating phase depend mainly on self-owned capital and reserved income. Because of their small scale of economy, they can hardly obtain loans from outsiders instituted. Low operating competence is another
cause. Though some small businesses have terrific performance, most small businesses struggle in the market because the technologies, facilities used in the small businesses are more obsolete compared to big businesses. Moreover, the service and products quality of SMEs ignites more complaints. In addition, low reputation is likely the key factor. Lots of small businesses ignored the importance of establishing high reputation in the capital market. In our survey, about 91% SMEs in creating phase have never acquired loans from commercial banks. If there is a good business opportunity, they have to raise fund from entrepreneurs themselves, their friends and relatives. From the liabilities of SMEs in developing and maturity phases, we can see that the percentage of long-term debt is low, current liabilities take a great deal of total liabilities. Moreover, current liabilities are made of accounts payable mainly. So we find that SMEs still cannot obtain enough capital from outer financing institutions. Therefore, the lack of financial resources lends to the poor reputation, physical resources, human resources, technological resources and organizational resources from the perspective of resource-based theory. In the finding we notices that SMEs commercial credit are mainly credit purchase for service and products and pre-accepted payment for new contract and new building projects. As to bank loan, we can see 70.21% of total SMEs have never acquired loans from commercial banks. The central government strictly supervises all kinds of finance institutes, puts on restrictions upon the development of small and medium-sized financial institutions and non-banking financial institutions, especially more restrictions on private financial institutions to avoid and cut down finance risk and stabilize the financial order. Some banks have obvious discrimination toward SMEs. For example, a few of commercial banks regulated that they would not make loans to the enterprises definitely whose registered assets are below 1million RMB. Due to the strict policy regulation SMEs can hardly issue stocks and bonds openly. They are also not obtained capital from some venture capital firms, such as angle investment.

3.4 Operating as sustainable suppliers in global supply chains

Herein is another advantage for SMEs: the ability to connect unaligned opportunities by becoming sustainable suppliers in global supply chains. Much of the literature to date considers the role of SMEs primarily as suppliers of larger companies. When SMEs produce unique sustainability technologies or processes, they can use their innovation potential to move their customers in the supply chain towards more sustainable directions.

SMEs should use effectively the self-capital whatever they are in any development phases, and do their best to put up the capital activity ratio, and utilize their trade liabilities, and then shut down the operating cycle. Of course, this status requires the enterprise to improve their adjustment in build and explore new projects and new marketing models. Because the large-sized companies have more integrate and complicated equipments, and the construct cycle is longer, and then leaves considerable space for the SMEs to develop. The SMEs can quickly explore new projects, transfer the technical production rapidly, supply more according to the market, and create more demand due to their flexible mercantile ways.

4 Discussion and Conclusions

We find that lots of SMEs have management defaults, especially in the aspect of finance management in China in our survey, Most SMEs have not established modern enterprise system and their operation decisions are often made by chief leader at will. Some even did not established financial system, so they rarely open their information to outsiders, and take their financial status as to business secrets. So the outer capital offers can't get full information about the SMEs, such as entrepreneur's management skill, the financial state, and the real usage of capital. It can be make the phenomena of asymmetric information between the SMEs and outsiders. Chinese financial systems have not created effective financing channels for SMEs by far. The external financing sources of SMEs still depend on state-owned or commercial banks gravely. For example, almost all of the state-owned commercial banks prefer to make loans to big business, and regard making loans to SMEs as to a venture investment. Most
commercial banks insist that making loans to SMEs have high risk, more complex procedure, high cost and low revenue per capita compared with making loans to big company. But in fact, it is the result of lacking of competitiveness of civil and foreign financial institutes and financial tools and services. Though almost all of provinces in China have established guarantee system for SMEs, because some of them were limited by capital scale, only a little of SMEs can obtained their guarantee supporting. Most of SMEs still were kept out doors by the banks because they fail to offer mortgages and effective guarantee. So relative government sectors should permit foreign finance institutes to operate RMB business as soon as possible. Because only in the pressure of competition, state-owned finance institutes could have the motivation of finance innovation includes the use of all kinds of finance tools, new finance markets and the development of finance service.

In summary, the paper finds that SMEs still cannot obtain enough capital from outer financing institutions. Lacking of financial resources lends to the poor reputation, physical resources, human resources, technological resources and organizational resources from the perspective of resource-based theory. The path of the SMEs’ sustainable development is changing SMEs financial status by improving operating efficiency and financial transparency and quickening reform and innovation of Chinese financial system; streamlining organizational processes and business models; operating as sustainable suppliers in global supply chains.

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