11-2021

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POLICY BRIEF
YOUNG ECONOMISTS' PERSPECTIVE
VOLUME VII, NO. 15, NOVEMBER 2021
ISSN # 2094-3342

De La Salle University
AKI
Angelo King Institute
for Economic and Business Studies

Small Fishes, Sharp Hooks: Obstacles to Economic Freedom Affecting Micro Small, and Medium Enterprises (MSMEs) in Southeast Asian Countries

Obstacles to economic freedom such as trade obstacles, finance obstacles, taxes, and corruption affect the ability of micro, small, and medium enterprises (MSMEs) to maximize firm performance. This policy brief is based on the observations made regarding the relationship of these obstacles to economic freedom in Southeast Asian countries Indonesia, Vietnam, the Philippines, and Malaysia. This will take into account the recent economic environment of each country.

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Policy Recommendations

Results exhibited the degrees by which MSMEs in each country find the obstacles to economic freedom an impediment to their performance. This is done by observing significant coefficients in regression. Insights derived from the estimation can then be utilized in policy formulation for the countries included. Hence the following policies are recommended:

1. Provide easier access to finance for MSMEs that are considerate of their limitations.
2. Provide resources for the improvement of the technical efficiency of MSMEs.
3. Implement zero tolerance for petty corruption.
4. Provide better tax incentives for MSMEs.

Introduction

About 90% of all enterprises are MSMEs, where they contribute roughly 50% of total global employment and 40% of national income in developing countries (Kituyi, 2020). With this, it is imperative to understand how obstacles to economic freedom are a determinant to MSME performance as a free economy incentivizes enterprises to be productive (Le & Kim, 2020).

The proponents pursued this topic with the intent of (a) determining significant firm-level obstacles to economic freedom that affect MSME performance amongst selected Southeast Asian countries, (b) comparing the effect of specified obstacles to economic freedom on MSME performance among selected Southeast Asian countries, and (c) providing policy recommendations with these findings.

Model Specification and Results

This study used trade obstacles, taxes, finance obstacles, and corruption as the primary variables of interest to analyze their effect on firm performance's economic freedom. MSMEs' profit is then used to measure firm performance, which is calculated as the firm's total annual sales minus their total annual costs. Moreover, age measures how long the enterprise has been in operation in years, whereas size classifies the firms into either micro, small, or medium, where small enterprises were considered the base category.

The OLS regression is utilized in the individual and all-variable regressions for all the countries except Indonesia, where the endogenous treatment regression is employed to address the proven endogeneity of finance obstacles in the country.

Table 1
Individual Variable Regression

	5.1.1 (trade)	5.1.2 (tax)	5.1.3 (corrup)	5.1.5 (fin)
Dependent Variable: Profit				
	Indonesia			
Minor	20.173***	20.818***	9.336**	-46.799***
	(4.982)	*(4.323)*	*(4.293)*	*(5.639)*
Major		-8.130***	-10.483***	
		(1.951)	*(2.316)*	
Constant		-3.941*		25.625***
		(2.305)		*(4.651)*
Observations	847	926	846	922
R-squared	0.14	0.161	0.125	
Prob > F	0.000	0.000	0.000	
	Malaysia			
Minor	0.601***	0.582***		0.509***
	(0.178)	*(0.180)*		*(0.154)*
Moderate	0.774***	0.926***	0.581***	0.818***
	(0.191)	*(0.175)*	*(0.201)*	*(0.17)*
Major	0.829***	0.634***		0.609**
	(0.233)	*(0.241)*		*(0.25)*
Observations	428	433	400	434
R-squared	0.066	0.077	0.07	0.07
Prob > F	0.000	0.000	0.0021	
	Philippines			
Moderate	0.582*	-0.550***		
	(0.347)	*(0.202)*		
Major	1.134***			-0.647**
	(0.419)			*(0.27)*
Very Severe				-1.136***
				(0.31)
Constant		0.548*	0.651**	0.629**
		(0.294)	*(0.309)*	*(0.297)*
Observations	557	617	503	607
R-squared	0.093	0.096	0.07	0.08
Prob > F	0.000	0.000	0.000	
	Vietnam			
Moderate				-0.408**
				(0.16)
Major	-0.786***			-0.407*
	(0.270)			*(0.21)*
Very Severe	-0.246**		-0.641***	-0.546***
	(0.120)		*(0.189)*	*(0.19)*
Firm Age	0.026**	0.025***	0.028***	0.023**
	(0.010)	*(0.010)*	*(0.010)*	*(0.010)*
Constant		0.326**		0.457**
		(0.156)		*(0.180)*
Observations	395	473	388	461
R-squared	0.104	0.087	0.091	0.101
Prob > F	0.000	0.000	0.000	

Robust standard errors in parentheses
**** p<0.01, ** p<0.05, * p<0.1*

The findings generally suggest that in the individual variable regression (a) Malaysia exhibited purely positive results in all regressions, (b) aside from finance obstacles, all variables showed mixed results in Indonesia, (c) aside from trade obstacles, which was positive, and corruption, which was insignificant, the Philippines had negative results, (d) Vietnam showed primarily negative results in all regressions except for taxation as it was insignificant, and (e) most positive results are consistent throughout all levels, whereas negative results tend to be more evident as the intensity of the economic freedom variable worsens.

Table 2
All Variable Regression

	Indonesia	Malaysia	Philippines	Vietnam
	Equation 5.1.7	*Equation 5.1.6*		
Dependent Variable: Profit				
Trade Obstacle				
Minor	17.264***			
	(4.402)			
Moderate	9.851*		0.823**	0.585
	(5.414)		*(0.400)*	*(0.479)*
Major	11.397*		1.057**	-0.890**
	(6.385)		*(0.463)*	*(0.368)*
Taxes				
Minor	19.455***	0.417*		
	(4.465)	*(0.248)*		
Moderate		0.545*	-0.723**	-0.306

		(0.289)	*(0.303)*	*(0.237)*
Corruption				
Moderate				-0.565**
				(0.25)
Major				-0.615***
				(0.22)
Very Severe				-0.876***
				(0.28)
Finance Obstacles				
Minor	-57.427***			
	(7.152)			
Very Severe	-	-0.697*	-1.030**	-1.030**
		-0.409	*(0.52)*	*(0.52)*
Firm Age		0.033***	0.024**	0.026**
		(0.01)	*(0.01)*	*(0.01)*
Firm Size				
Micro			-0.460*	
			(0.25)	
Medium	20.986***		0.955**	0.759***
	(3.39)		*(0.43)*	*(0.26)*
Constant	26.487***	-0.624**	0.586	0.409*
	(5.54)	(0.25)	*(0.38)*	*(0.23)*
Observations	762	373	428	323
R-squared	-	0.106	0.12	0.135

Robust standard errors in parentheses
**** p<0.01, ** p<0.05, * p<0.1*

Compared to when each individual variable was regressed, the number of significant results had decreased when all four economic freedom variables were regressed together in each country and that finance obstacle and corruption had entirely gotten negative results, whereas taxation and trade obstacle had gotten mixed results.

Through this, it was determined that financial obstacles are significant obstacles to economic freedom that negatively affect MSMEs for all of the observed countries. Therefore, policy formulation should look into the restrictions that financial institutions unknowingly impose on MSMEs with these firms' limited resources. For instance, financial institutions often require audited financial statements to apply for a credit line, which could be costly for these firms. Therefore, it is necessary to provide easier access to loans, credit lines, and other forms of financing that are considerate of MSME limitations.

Trade obstacles in Indonesia, Vietnam, and the Philippines were found to positively impact firm performance, which indicates that firms benefit from trade regulation. Briefly investigating the export activities of the MSMEs in these countries, it was revealed that these smaller-sized firms are less likely to participate in the exports market. Hence, trade obstacles had a positive effect on firm performance as less liberalized trade would decrease the entry of competitive foreign firms. Restrictive policies would be detrimental in the long run; therefore, improving export competitiveness among these firms would allow them to maximize the loosened restrictions in inter-country trade while improving their country's trade balance. Policy formulation for this should then take a deeper look into how exactly MSMEs are affected by the factors involved in trade liberalization policies. Hence, provisions of resources that would improve the technical efficiency of MSMEs would include better infrastructure, internet connectivity, and access to technological advancements in production.

Corruption is evident in both Vietnam and the Philippines; however, the obstacles it imposes at the firm level are only significant in Vietnam. Policy formulation for this should include analyzing which levels and aspects of corruption affect MSMEs as well as ways to disincentivize such behavior among parties involved. Particularly, this sheds light on petty corruption, which is a form of corruption that affects firm-level proponents. It often involves bribery between firms and the public sector, as well as withheld resources meant for firms that are redirected to public sector officials intended for personal use or gain. Hence, policies that mitigate petty corruption are necessary.

Given that tax burden had been seen as a significant obstacle for MSMEs in the Philippines and Indonesia, levying better tax incentives to smaller-sized firms could lead to better-performing firms. Hence, policy formulation for this would require a deeper look into how taxes impose detriments on MSMEs considering their limited resources. Excess income from reduced tax burden would lead to higher profit margins. Particularly, tax incentives would include the reduction of taxes for MSMEs, tax holidays, and special tax considerations for MSME start-ups.

Conclusion

The obstacles to economic freedom pursued in the study presented mixed results. Finance, corruption, and tax had exhibited overall negative effects on MSME performance. On the other hand, trade obstacles mostly exhibited positive effects on MSME performance as the majority of these firms did not participate in exports. Hence, it is crucial in policy formulation to factor in these results as they provide evidence that economic freedom benefits MSMEs, whereas obstacles to economic freedom deter these enterprises in Indonesia, Malaysia, Vietnam, and the Philippines.

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This publication is based on an undergraduate thesis for the Economics program of the School of Economics of De La Salle University.