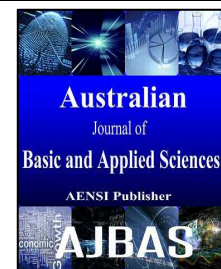




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### Corporate Governance in Malaysian Tourism Small and Medium-Sized Enterprises: Review of Research Issues

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#### ABSTRACT

Background: Tourism small and medium-sized enterprises (SMEs) currently emerge as one of the world's major enterprises with significant changes in its structure and operation. As for Malaysia, the continuous efforts to stimulate the tourism industry by the Malaysian government have created a positive effect on the business activities of SMEs. However, many studies emphasize the problems in managing SMEs in terms of corporate governance for instance lack of awareness on corporate governance structure, lack of awareness on corporate governance operation, size of the board, lack of industry expertise and strategic vision. Objective: This paper presents a general review of the research issues regarding the matter as the first step to enhance further research. Results: The review from related articles indicated that there are three major research issues on corporate governance in SMEs which can also be discussed in the tourism industry. These issues were identified as the roles of corporate governance, the challenges of corporate governance and the significance of corporate governance to SMEs. Conclusion: These three issues should be given serious attention by scholars in determining specific area to be investigated within the context of tourism SMEs. Further, the issues also contribute in terms of practicing corporate governance toward managing tourism SMEs effectively.

#### INTRODUCTION

Tourism industry in Malaysia has become the second major contributor to the nation's Gross Domestic Product (GDP) and is now one of the fastest growing sectors in the Malaysian economy with a major contributor to foreign exchange earnings in the country. As tourism emerged as one of the world's major industries with significant changes in its structure and operation of the tourism industry worldwide, the global transition to tourism-focused economies, the emergence of new destinations, and increasing demands for differentiated tourism products and services have engendered the need for tourism small and medium-sized enterprises (SMEs) to develop strategies to become competitive in the changing global economy.

Tourism SMEs performance and survival in the industry are particularly important to Malaysia because apart from their key role in delivering tourism products to the tourist, they also play an active role in advancing the local community (Ateljevic, 2009; Buhalis and Law, 2008; Getz and Carlsen, 2005; Page, Forer and Lawton, 1999). Despite the efforts, tourism SMEs still continue to face challenges that impede successful tourism development in destination countries, thus slowing gains that can emerge from tourism SMEs activities. The Malaysian government has stimulated continuous efforts to create a positive effect on the business activities of

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tourism SMEs for instance by creating business potential and developing diversification of tourism products and services.

Malaysia has come out with various tourism SMEs programs and policies implemented by the government to promote the Malaysian tourism industry. As reported by the Small and Medium Enterprise Corporation Malaysia (2012), the government spent RM 4,677.1 million in the form of 183 training and financial programs for tourism SMEs in 2011, thus increasing the funding on the development allocation. Eventually, this indicates that the government has placed high expectations on tourism SMEs to play their role as a vital component in increasing the country's foreign exchange earnings.

Tourism SMEs in Malaysia employ about 991, 419 workers accumulate to 38.1 per cent of total employment in SMEs services sectors. As a matter of fact, the tourism industry employs more than a third of employees in the services sector and is considered the second highest earner in foreign exchange and national income. Taking into account that tourism SMEs in Malaysia play significant role in the economic development of the country with 239,110 active establishments including 142,721 firms (59.7 per cent) offering food and beverage services, 40,025 firms (16.7 per cent) offering transportation services and other miscellaneous tourism services and 19,643 firms (8.2 per cent) offering accommodation services; arts, entertainment and recreation services; and travel agency, tour operator and tourism guide services, it is important to explore and understand the related issues concerning corporate governance in tourism SMEs.

Many studies emphasize the problems in managing tourism SMEs which are related to corporate governance for instance, lack of management, lack of industry expertise, have a shortage of financial resources, lack of marketing skills, and lack of strategic vision (Thomas and Augustyn, 2007; Augustyn, 2004; Beaver, Shaw and Williams, 2002; Boer 1998; Dewhurst and Horobin, 1998; Friel, 1998; Wanhill, 1998; Webster, 1998). Hence, in order to ensure that the SMEs are able to play an effective role, Muhd. Yusuf, Din and Jusoh (2014) suggest that there is a need to look for more ways to improve the performance of SMEs in order to enable them to help the country boost its economy to achieve the aspirations of becoming a high-income economy nation.

#### ***Understanding SMEs in Tourism Industry:***

There have been few studies investigating different segments of SMEs (Jaafar, Maideen and Sukarno, 2011; Dewhurst and Horobin, 1998). However, an intensive literature review also reveals that there have been very few studies on tourism entrepreneurship and small businesses in the tourism industry. This is probably due to the fact that entrepreneurs in the industries might possess lower levels of entrepreneurial characteristics compared to other industries. Additionally, several studies indicate that most tourism entrepreneurs begin tourism SMEs due to the low entry barrier in the industry (Brouder and Eriksson, 2013; Skokic and Morrison, 2011; Morrison and Thomas, 1999).

Further, Mazzarol, Volery, Doss and Thein (1999) and also Skokic and Morrison (2011) suggest that the owner-manager's socio-economic characteristics such as age, gender and education level also form a part of the obstacles that have a considerable effect on entrepreneurial intention and business performance of SMEs. Several studies also found that information technology has also become barrier for successful SMEs (Lim, Baharudin and Trakulmaykee, 2015; Alam, Ali and Jani, 2011; Omar, Mohamad, Marimuthu and Ramayah, 2011).

Generally, the literature in tourism SMEs suggests that co-operation appears to be a vital option in their survival and possible growth. Few researchers agree that the exchange of information, research as well as joint marketing facilitate product development and expansion of markets beyond the local area (Thomas and Augustyn, 2007; Augustyn, 2004; Beaver, Shaw and Williams, 2002). Further, it is also suggested that tourism SMEs cooperation is needed at the destination level in order to increase the competitiveness of SMEs and their respective destinations as well as to facilitate higher customer satisfaction (Buhalis and Cooper, 1999).

#### ***Good Corporate Governance Mechanisms:***

According to Denise and McConnell (2003), Denise (2001) and Weston, Chung and Hoag (1990), various mechanisms are applied within the models of corporate governance in order to encourage managers to pursue goals that are considered desirable. The mechanisms are generally divided into two, external and internal where both may determine the effectiveness of corporate governance. The mechanisms that operate outside the firm are the legal and regulatory frameworks and competitive markets which are taken by organizations as a given framework. On the other hands, mechanisms operating within the firm are bonds (contracts), performance-based incentives and monitoring mechanisms such as the board of directors, debt and the ownership structure (Denise and McConnell, 2003; Denise, 2001; Jensen, 1993; Jensen and Meckling, 1976).

In contrast, internal mechanisms are, in principle, more flexible than external mechanisms and can be varied by shareholders as circumstances dictate. These mechanisms are argued tend to be use by firms depending on the characteristics of the firm's operating environment. External mechanisms further influence internal mechanisms. As noted by Denise (2001), the external and internal division of the mechanisms is conceptually

useful for focusing on each of the mechanisms and assessing its effectiveness in addressing the incentive problem.

### ***Objective of the Paper:***

Many firms and organizations believe that good corporate governance could greatly impact specifically on the internal operations which involve four main aspects including strategic direction, financial expectations, transparency issues and shareholder activism. These aspects can also be applicable in the context of tourism SMEs. Hence, the major purpose of this paper is to review previous related articles on the issues of corporate governance in SMEs as to develop conceptual framework towards better understanding of the context within the tourism industry.

### ***Review Of Research Issues:***

#### ***The Roles of Corporate Governance in SMEs:***

The contribution of SMEs in the development of world economy has been significant, both in terms of contribution to GDP and creation of employment opportunities. Additionally, SMEs have played a remarkable role in the development of several countries as they constitute a major part of the industrial activity both in developed or developing economies. Moreover, Pandya (2012) also notes that more countries can boost their growth by strong SMEs for example Taiwan and Japan. Moreover, Columbia is also seen as country having high economic growth guided by dynamic SMEs. It is emphasized by Tambunan (2008) that SMEs play a vital role in economic development, as they have been the main source of employment generation and output growth, both in developing as well as in developed countries.

In developing countries, the roles of SMEs become more crucial as they have potential to improvement of income distribution, employment creation, poverty reduction and export growth. It also leads to the development of entrepreneurship, industry and the rural economy. Hence, it is very important to apply corporate governance practices in SMEs. One of the major roles play by the corporate governance is to make room for the composition of a board which will include external directors not necessarily linked to the owner and thus induce more independent best practice methods of running the business and attaining profits. A study by Abdul Manaf, Amran and Zainol Abidin (2014) regarding the size of Board in relation to accounting conservatism reveals that board of director is more effective when the number of board members is small.

The governance subject has often been considered was acknowledged as a major problematic issue affecting that touches all types of enterprises particularly the SMEs (Hamad and Karoui, 2011). In fact, it is more specific to the context of small and medium size firms than that of large enterprises. Looking at the perspective of an entrepreneurial firm as SME, it is believed that there is a need to access resources for growth. They need inputs on business operations, good strategy and best practices in the industrial sector. Also, as entrepreneurial firms grow, the need to introduce professional governmental practices and managers arises. Table 1 summarizes the corporate governance roles in SMEs.

**Table 1:** The Roles of Corporate Governance in SMEs.

Issues of Corporate Governance Roles
1. Composition of a Board
2. Induce more independent best practice
3. Access resources for growth
4. Introduce professional governmental practices

#### ***The Challenges of Corporate Governance in SMEs:***

Several studies also noticed that SMEs have to struggle with few challenges in order to perform and compete with other industries. Success and failure of SMEs are not only related to only the financial aspect, but also depends on the characteristics of the entrepreneur and many more key strategic factors (Menefee, Parnell, Powers and Ziemnowicz, 2006). It is noted that due to small size, series of problems are also encountered such as lack of finance, low human resource capabilities, and technological capabilities (Hussain, Farooq and Akhtar, 2012). Apart from this, other corporate governance practices such as poor management competences, lack of skilled manpower, deficiencies in marketing strategies, low efforts on research and development and lack of innovative technology are also prominent factors responsible for unstable growth of SMEs (Grimsholm and Pobleto, 2010).

Another important factor responsible for SMEs is lack of corporate governance structure in firm (Mahmood, 2008). It is understood that usually there is a lack of awareness among these enterprises regarding significance of corporate governance. Furthermore, insufficient access to financial resources and investment capital are significant barriers to growth for SMEs (Tung and Aycan, 2008). Previous studies have also highlighted the profound challenges faced by SMEs in other industries that affect the survival of their businesses during the start-up phase for example, a lack of management practices in the entrepreneurs regarding the

creation of a business plan as a worthwhile activity, not engaging in business networking and a poor rate on internet adoption (Tan, Chong and Uchenna, 2009; Alam, Ahmad, Abdullah and Ishak, 2007; Junaidah, 2007; Hall, 1995).

Besides, as noted by Reynolds and Miller (1992) one of the key factors for fully developed new firm is the full time commitment of one or more individuals. Many researchers agree that human resource factors form one of the most significant areas for success of a company (Conner and Prahalad, 1996; Spender, 1996; Lei and Hitt, 1995; Castanias and Helfat, 1991). Study has reviewed marketing limitations of SME as limited resources (such as financial, time and marketing knowledge), shortage of exclusive marketing techniques, and limitation in market influence (Latini, 2011). Table 2 presents the challenges of corporate governance in SMEs.

**Table 2:** The Challenges of Corporate Governance in SMEs.

Issues of Corporate Governance Challenges
1. Specific characteristics of the entrepreneur
2. The size of the organization
3. Lack of corporate governance structure
4. Insufficient access to financial resources
5. Insufficient access to investment capital
6. Lack of awareness on corporate governance matter

### ***The Significance of Corporate Governance to SMEs:***

The significance of corporate governance cannot be over emphasized as it creates the necessary organizational setting for the internal operations of a business enterprise. In fact, it is believed that corporate governance would benefit SMEs in several aspects. For instance, the implementation of corporate governance among SMEs can result in better management practices, stronger internal auditing and greater opportunities for growth. Similarly, good corporate governance practices assist SMEs in improving on their prospects of obtaining funding from investors and financial institutions.

As noted by McGahan and Porter (1997), applying good governance principles reduces the problems associated with information asymmetry and makes the SME less risky to invest in. Dube, Dube and Mishra (2011) reported that good governance improves SMEs' prospect of obtaining funds from banks, investors and venture capitalists. They also contend that firms that have greater transparency or information disclosure tend to have healthier growth rates and ratios of ordinary profits to that of capital, than firms who do not do so. Research on listed firms has shown that strategy influences corporate performance and external board members (Pettigrew and McNulty, 1995). Thus the existence of external board members could lead to better management decisions and help SMEs to attract better resources.

Corporate governance also has a role in SME performance since it improves transparency and attracts capital at a cheaper cost (Spanos, 2005). The lack of proper governance mechanisms have been attributed for the failure of state owned enterprises thus this phenomenon may well cripple the effective development and growth of SMEs. Therefore, it is important then for proper management of this sector to ensure enhanced performance.

The board of directors represents the main organ of control, complementary to the external mechanisms. The role of the board spreads to several functions within the SME: the administration of the enterprise, regaining some roles of surveillance, control of the directors and the setting up of the enterprise strategy, the organization of relations between the enterprise and its environment, the capitation of the external facilities, the recompense the directors, dismiss them, and ratify and control the important decisions making by the direction (Van, Heuvel and Voordeckers, 2006). Table 3 indicates the significance of corporate governance to SMEs.

**Table 3:** The Significance of Corporate Governance to SMEs.

Issues on the Significance of Corporate Governance
1. Better management practices
2. Stronger internal auditing
3. Greater opportunities for growth
4. Better prospect in obtaining fund
5. Improve transparency
6. Attract capital at cheapest cost

### ***Conclusion:***

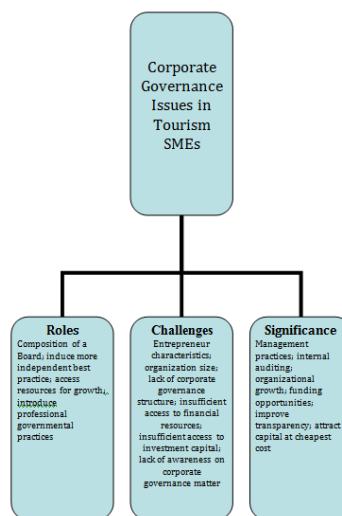
#### ***Discussion on Corporate Governance in Tourism SMEs:***

Today, many firms and organizations including tourism SMEs are practicing a good governance mechanism to increase their performance (Denise and McConnell, 2003; Denise, 2001; Weston, Chung and Hoag, 1990). The SMEs are now improving their corporate governance practices knowing it increases valuations and boosts the bottom line. The adoption of best practices in corporate governance particularly in the Malaysian tourism SMEs has a prominent place in the regulatory and developmental global agenda of the country capital markets. Furthermore, the enforcing of corporate governance practices result in strict and stringent mechanisms which could dampen corporate entrepreneurship.

Due to the fact that the tourism SMEs play a crucial role in the tourism industry by delivering tourism products and services to the tourist, vigorous efforts have been made by the Malaysian government to utilize the advantages that tourism SMEs can offer. Given that tourism SMEs performance and survival in the industry are particularly important to Malaysia because apart from their key role in delivering tourism products to the tourist, it is therefore essential to observe tourism SME performance to ensure the industry will reach their full potential through playing an active role in advancing the local community.

### Conclusion and Suggestions:

Having reviewed several related researches on corporate governance in SMEs, this conceptual paper concludes that there are three major research issues which significantly can be discussed in the context of tourism industry (Figure 1). The issues are known as the roles of corporate governance, the challenges of corporate governance and the significance of corporate governance to SMEs (Hussain *et. al.*, 2012; Pandya, 2012; Grimsholm and Poblete, 2010; Tambunan, 2008). These issues need to be further investigated to understand and determine the key success factors of tourism SMEs and at the same time recognizing the important of tourism SMEs. Hence, it is therefore pertinent to ensure tourism SMEs will survive the various challenges to reach their full potential.



**Fig. 1:** Conceptual Framework of Corporate Governance Issues in Tourism SMEs.

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