

# INNOVATION IN VSMEs OF PAKISTAN: WHAT NEXT!

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**Abstract:** SMEs play a vital role in the most developing and developed nation. His role in the development of the economic growth and sustainability has been widely recognized. Due to its importance much emphasis has been put in through research and publication. Most research has covered on the characteristics of SMEs, its role in the economic development and its challenges in today's competitive world. Consequently this paper focus on the uniqueness of the technology base SMEs. This study mainly focus on those SMEs which having informal structure, micro in size, located in remote and rural areas and work force are up to five persons, which after this will be called at Very Small and Medium Enterprises (VSMEs). It described the capability of these VSMEs to innovate and retain their competitiveness. Its therefore suggest a conceptual framework for the VSMEs as in input to the Government to provide funding and training on more effective and efficient manner.

**Keywords:** Invention, SMEs, Sustainability, Scarce Resources, VSMEs,

## INTRODUCTION

**S**MEs play a vital role in the development of economic growth and sustainability. Due to their sheer numbers, size and nature of operations, this fragment is the back bone of

Pakistani economy. The SMEs are a proficient user of the scare resources and domestic products, and has better linkages with other sectors of domestic economy [1-2]. Pakistan has emerged as the second swiftly growing economy in Asia after China in 2004 – 2005, as claimed by government of Pakistan and well accepted by international raters and financial institutions [3]. The prospective SMEs promote domestic led growth in new and existing industries. To strengthen the flexibility of the economy in a competitive and challenging environment are inarguable. In Pakistan, the important role of SMEs is clearly indicated by research and statistics. In 2009-10, a period during which real GDP of Pakistan grew by 3.8 percent, the small-scale sector provided much support to overall growth by 7.5 percent. Thus, it is clear that in times of economic recession, SMEs outperform than large enterprises providing much support to overall economic growth [4].

The 99% of establishments in Pakistan are SMEs. From this more than 96% SMEs are less than five Employees, (SMEDA, 2005). These are involved in business of trade, wholesale, retail, restaurants, service sector, and manufacturing [5]. So it is more appropriate to call these SMEs as VSMEs. There are so many challenges faced by SMEs. For instance, even in defining SMEs, it is very difficult to define SMEs in Pakistan because most of the organizations

define SMEs according to their own needs and interests. Financial institutions, public sector organization, non-governmental organizations (NGOs), international organizations, researchers and SMEs services providers have their own definitions based on their own criteria selection [6]. Most of these authorities and organization used various terms for SMEs such as Small and Medium Scale Industries (SMIs), Micro Enterprises (MEs), Rural Enterprises (REs), Small and Medium Scale Activities (SMAs), Cottage and Small Scale Industry (CSSI), Informal Sector Activities (ISAs), Micro and Small Scale Activities (MSSA), etc. [7].

Government of Pakistan establishes Small and Medium Enterprise Development Authority (SMEDA) in October- 1998 to enhance and develop this sector. When we think about SMEs, we consider it as one-person manufacturing enterprise but according to SMEDA Small Enterprises should possess ten to thirty five (10-35) employees with two to twenty (2-20) million rupees capital intact in equity. Medium Enterprises should possess thirty six to ninety nine (36-99) employees with twenty to forty (20-40) million capital intact in equity [3]. Chew (1988) defines small businesses as: tiny establishments – firms with 5-9 workers. Small establishments contain with 10-49 workers and medium establishments with 50-99 workers [8]. The VSMEs are even not defined by the controlling authority. There are many organizations, and institutions involve in development and promotion of SMEs in Pakistan, but overall coordination is very poor among them. The establishment of SMEDA as an apex body is to development and promotes this sector. But still most SMEs promotion bodies not under SMEDA [9]. However, the under consideration class i-e VSMEs completely ignoring by controlling authority. The purpose of the study is to boost up the problems of the most deprived and helpless class of SMEs. And set a paradigm for the researchers, Business practitioner and governmental authorities. Instead of the above troubles, these unique characteristic holders and very special type organizations are courageously facing the problems. They are still surviving in the realm of business and added their contribution to the employment generation, economic growth and sustainability.

#### **INNOVATION IN SMEs**

In order to be successful in business and to sustain its operations, the entrepreneur or small business manager needs to have an innovative frame to compete against large organizations. Well-known entrepreneurship scholars support this concept by arguing that innovation is essence for entrepreneurship [2]. Malecki and Poehling (1999)

demonstrated strong evidence that customers, suppliers and other firms are the most versatile source for focusing on innovation. The general public attributes greater promise that smaller firms investing heavily in innovations than larger organizations [10]. To stay and survive in increasingly high competitive markets, innovation is the only solution. Focusing on innovation is the best policy [11]. Most of the researchers suggested that innovation orientation and innovation activities create value for both new and established SMEs. Nevertheless, innovation can involve high initial and continuous investments, risks, and uncertainty, on the other hand it provides best from competitor, customer loyalty. Price premiums for innovative products and entry barriers for potential copycat generally seem to outweigh the costs [12]. Not surprisingly, for the big idea that promises entrepreneurial success is identification of a basic innovative offering, production process, and/or business model. Innovation is a process where individual's forms associations based on expertise and skills for translating ideas into concepts and models [13]. Innovation has a positive effect on the performance of SMEs. To maintain and sustain their economic development it is necessary to focus more on innovation [14]. Most of the larger enterprises today have their origins in small and medium enterprises. However, SMEs lack of the research capacity, the ability to take significant risks, or any other advantage of expansion. Innovative SMEs are those that identify, interpret and apply knowledge effectively throughout the organization [15]. Some literature proposes that smaller organizations can profit by adjusting and changes faster than a large organization due to their missing hierarchies and quick decision-making. The smaller, scarce resource firms are found more likely to benefit from pursuing innovation [12]. In a nutshell, no company can survive unless and until they innovate. Thus, there is a need to further investigate and deeply studied the whole structure of these unique characteristic holder companies, and how these VSMEs become innovative. So in the next we are discussing about the characteristics of SMEs and VSMEs.

#### **CHARACTERISTICS OF SMEs.**

Before we characterize the VSMEs, it is prominent at this level to understand the basic characteristic of the SMEs. A proper understanding is needed while focusing on Special type of SMEs. Ghobadian and Gallear (1997) listed some basic characteristic of SMEs, i.e structure, behavior, process, and procedure. However, to study Yousaf and Aspin wall (2000), Wong and Aspin wall (2004), D'Amboise and Mudowney (1998), Haksever (1996), and Spence in (1999) have help to compile a list of characteristics of SMEs [16-21].

**Table 1.** Comparison between SMEs and VSMEs.

S.No	Characteristics	SMEs	VSMEs
1	<b>Ownership and Management Structure.</b>	1) Mostly run and Managed by Owner but some organizations have the managerial position. 2) Sometimes partnership Business. 3) Employees up to 250 Persons 4) Mix Products and services	1) Run and control by the Owner 2) No. Partnership concept 3) Employee up to 05 persons 4) Mono Products and services.
2	<b>Systems, processes and procedures</b>	1) Planning and control system 2) Informal rules and regulation 3) Focus on process and products 4) Expert in sharing inherent knowledge.	1) No. Planning systems 2) No. rules and regulation 3) Mainly focus on production 4) Doing business on family tradition
3	<b>Customers and Markets.</b>	1) Close relation with Customers 2) Focus on Local, regional and International markets	1) Close relation with customers 2) Cell to Super Local market
4	<b>Culture and behavior</b>	1) Informal and Unified cultural 2) Departmental specification 3) Behavioral of employees influenced by owner manager decision	1) Special and unique culture 2) No. specification of departments 3) Owner can making decision on his own willing and needs.
5	<b>Human capital Management.</b>	1) Lower degree of job specification 2) Expert in each departments	1) Lower degree of job specification 2) Mostly one person show that hold the minimum expertise.

### **Ownership and Management Structure**

Most SME owners act as owner-managers and also play the part of the company's strategic initiator. A flatter organizational hierarchy in SMEs leads to greater flexibility in work but due to limited or less clear division of responsibilities. This means that top management is near to operational functions. Decision-making is generally centralized and the ultimate power of control lies in their hands. The decision making channel is shorter in SMEs. There is a lower degree of job specialization with more generalists. Communication lines are shorter, which allows for easier and more direct information flow. Thus, the owner- managers enjoy highly visible in the organization. This structure leads to higher levels of coordination and cooperation [17].

### **Systems, processes and procedures.**

SMEs have simple planning and control systems. The procedure and rules are informal. There is less consistency of work processes. The operations are less complex. Processes are more fluid and are adjustable to various situations. SMEs also have a narrow scope and mostly focus on operational, rather than strategic, processes and knowledge creation.

They are more expert at sharing inherent knowledge [22-23].

### **Customers and Markets.**

Mostly, SMEs depend and focus on a small customer base and local or regional markets, with a few international markets. They usually have limited product/service lines and sometimes supply to niche markets. Employees have close relationships with their customers. Customer satisfaction is one of the main criteria in measuring performance. Moreover, because of the closeness of relationships, specific requirements of the customer are more easily understood [16-23].

### **Culture and behavior.**

SMEs usually have an informal and unified culture. The size of the organization fosters recognizing the company as a whole instead of looking at single departments or functions. The behavior of employees can easily be influenced by the owner-managers' decision. So there is an open culture trend in SMEs. In open culture, employees have to work independently not only enables the knowledge creation but can be easily transferable in the whole organization [16-23].

### **Human capital Management.**

A limited number of expert personnel, human capital are an important resource, and high turnover rates can severely affect operations. Since SMEs have fewer clear employee responsibilities, a lower degree of job specialization occurs, leading to greater employee turnover. Human capital development is done according to specific needs. The performance evaluation is not standardized [22-23].

From the above characteristics of SMEs, now we have to sketch and catalog of the characteristic of Special and unique characteristic holders', i.e VSMEs, The following table shows clear difference between SMEs and VSMEs.

### **METHODOLOGY**

Data were collected from various secondary sources such as Research Papers, various reports of SMEDA, Annual Economic Survey of Pakistan, and Business News providers, etc.

### **DISCUSSION**

Every researcher and authority are trying and focusing on SMEs to enhance their capability to be more competitive. The encouragement of small-scale enterprises can help in achieving many objectives, and in particular. It can help in reducing the problem of wide-spread unemployment in Pakistan [24]. The general assumption is that small industry can set up with small capital, and can produce goods for domestic consumption by using labor intensive technology. This study is basically for the deprived class of SMEs. It suggested that VSMEs should innovate and develop in this challenging economic world. This class is located in rural and remote areas. In addition, they don't know about innovation, technology and sustainability. They are just reflecting other firms that are located in the same area. They are living with the principal of hand to mouth. If we talk about sustainability, "Profit, People and Plant" are the main ingredient of sustainability. But the concept for VSMEs is not even in place. The informal sector consisting of small enterprises and household units expand more quickly than the formal sector. This can add great contribution towards employment to the poor people of Pakistan [25]. These businesses running from the Stone Age and still they contribute to Employment generation, poverty reduction and sustainability in his own realm. The dynamic growth of this sector has taken place because the state and its authorities have kept away from it and let it function largely on its own [26]. Necessary Efforts is needed to boost up this sector for both employment, GDP growth and to organize its financial behavior. VSMEs are vital for world prosperity. Collectively they are the largest employers and greatest creators of wealth in Pakistan.

### **INNOVATION TREND IN VSMEs**

Majority of the entrepreneurial knows that in order to survive, their organizations have to continuously focus on surrounding and improve their way of doing business. The interest in innovation adoption has occurred in all organizations i.e small or large firms. However, small firms are less likely to adopt the innovation due to scarce resources and the effort involved, while we know that organizational size affects innovation adoption [6]. Innovation is continues the process for growth and sustainability. Focusing on current and future competition the organization has to invest heavily on research and development. Shahid Yousaf argued that any organization that needs growth ready to invest 2% to 3% on R&D. Entrepreneurial, and managers are taking great interest in the adoption of innovation because of the essential role innovation plays is securing sustainability [1]. All researchers are agreed and argue that a country will lead in the 21<sup>st</sup> century that focusing and invests on innovation. From the literature, it is concluded that innovation is necessary for all kinds of business who want to stay. Government policies give more importance to the formal and large-scale sector, and it received special privileges [27-28]. As a result the VSMEs are neglected despite their important role in the economic development. Thus for the survival and sustainable growth of these special types VSMEs the Government has to support, provide education on future perspective, strategic and financial assistance on a war footing and revolutionary basis. From the above it is concluded that unless and until the VSMEs are promoted, the dream of economic revival may not come true.

### **FINANCE/ CREDIT CONECEPT IN VSMEs**

Small business can be set up with small capital, and can produce goods for domestic consumption by using labor intensive techniques and technology. In Pakistan adult literacy rate is 48% and majority of entrepreneurs operating small businesses and industry are not educated. And as such they hesitate in approaching small and medium enterprises development authority and banks for loans [29]. Credit/ Financial support is the main problem of VSMEs in rural and remote areas. Most of the financial institutions are not willing to finance this informal sector. The related agencies and institutions have limited access to a rural area. The owners of VSMEs do not know about the processes and documentations of loan. These institutions discriminate against VSMEs because they are considered high-risk clients. Khalid Nadvi in his survey of 328 small-scale enterprises found that only 2 (two) of them had been able to obtain credit from

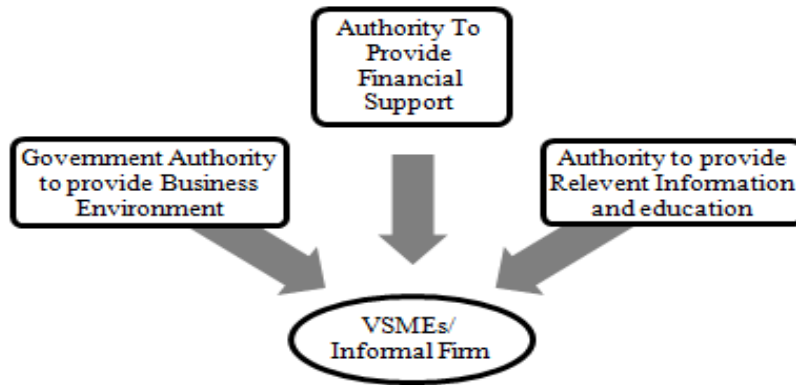


Figure: 1 Showing Initial Stage

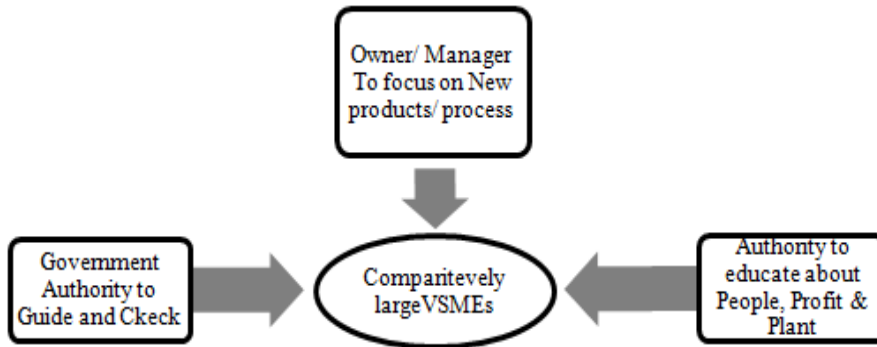


Figure 2: showing the Monitoring stage

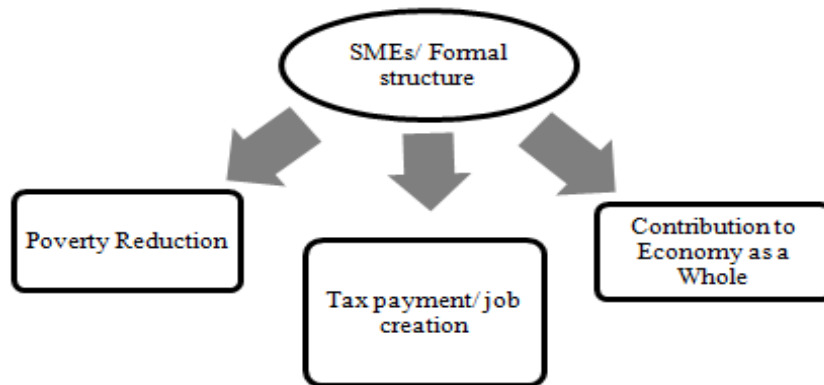


Figure 3: Showing the Maturity Stage

the formal banking sector, and both loans were of very small amounts [26]. Access to finance is a big problem for VSMEs in Pakistan. Most entrepreneurs have to rely completely on their own savings and money borrowed from friends and relatives.

**APPROACH TO SUSTAINABILITY IN VSMEs**

A Business is called to be sustainable or green business, if there is no negative impact on the global or local environment, community, society, or economy. John Elkington in his introduction of his

book, "Cannibals with Forks" (1998), stated that doing business must be according to financial, environmental and social returns. This is now commonly called the "triple bottom line. Crals & Vereek, (2005) Define 'three Ps' People, Plant and Profit as the concept of sustainability [30]. If the above three aspects has satisfied before an entrepreneurial activity to be labeled as sustainability. In the realm of VSMEs a sustainable business is that who are produce more and more for a short run. They are not focusing on environment nor on society but mainly focus on profit. The basic problem of Pakistan industrial structure is concentration in the few low value added industry categories. So this is a big hurdle for sustainability of VSMEs. The complexity of the governmental SME supports institutions worse the situation. It should be simplified and to become customer-friendly. The government can implement regionalization with centralization and uniformity with diversity in their SME supportive systems. The decentralization of governmental SMEs supportive organizations and structure may be good to provide more flexible, responsive and customer-driven service to the informal sector, i.e VSMEs who badly needs business development assistance [6]. It is suggested that government has to educate and provide a supportive environment for these VSMEs

#### CONCLUSION

From the above literature review and discussions, it is concluded that a frame work is needed for the growth, survival and sustainability of VSMEs. This conceptual model is proposing for the Rural and remote areas of Pakistan. The main purpose of this conceptual model is to develop and sustain the deprived and helpless class. That becomes viable to produce and adopt environmental friendly and commercially viable product and process on a sustainable basis. The frame work distributed into three stages as discussed below.

#### INITIAL STAGE

In the initial stage, the Governmental agencies need to provide three major support for the VSMEs

1. Financial Support to Business (2) Environmental Support (3) Awareness of the Existence

First, the government has to arrange for the fund. i.e financial support is the key success of the firm. The second is to provide a business environment that entrepreneur can easily produce and marketing their products and services. Most of these special type organizations are own and managed by the illiterate people. With the combination of these two authorities, the governments also have to make arrangements for the educational growth of the entrepreneur. Fig -1 further elaborate the initial stage.

#### MONITORING STAGE

In this stage, the VSMEs is comparatively Large and the need of Governmental authority to monitor. This is a monitoring and moving stage for the entrepreneur as well as organizations. In this stage, the firms are growing and moving so its need some feeding. The feeding in this stage is that the authority has to start education about People, profit and plant, which is the philosophy of sustainability. In this stage, the owner/managers are also aware of the surrounding of business, so this is the right of the operator to focus on new products and process. In this stage, the VSMEs have established and moved towards the economy as established SMEs. Hence, it has significantly played the role to the economic development of Pakistan. Fig-2 further elaborates the monitoring stage.

#### MATURITY STAGE

This is a time to cut the ripe fruits, so we also called this a harvesting period. In this stage, the firm becomes formal in structure and now we called it SMEs. So in this stage it is a responsible firm and knows his duty very well. Fig.1 clearly shows his involvement in the form of Poverty reduction, job creation, tax payment and contribution to the economy as a whole.

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