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Innovation and SMEs' Performance: The Case of Lao PDR

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Introduction

- SMEs are crucial part of the Lao economy and livelihoods. They account for 99.8% of total enterprises and more than 80% of total employment in the business sector.
- They have gained increased attention from the government in recent years, considering their economic importance.
- Generally, SMEs in Lao PDR face the constraints, including lack of research & development, innovative activities, mainly due to financial access constraints.

Introduction

- In recent years, literature on innovation in SMEs has drawn attention by researchers; for example Intarakumnerd & Goto (2016) for East Asia; Pachouri & Sharma (2016) for India; Pham & Ho (2017) for Vietnam; Le *et. al.* (2022).
- Limited studies on the factors influencing innovative activities in SMEs in Lao PDR as well as the relationship between innovation and SMEs performance.
 - Sisounonth & Chansomphou (2023) examined the factors influencing innovation in SMEs in Lao PDR and suggested that manager's experience, access to finance, training, direct export, income and having their website, have positive impact on innovation.

Objectives of the Study

- To investigate the factors influencing innovation in SMEs; and
- To examine the relationship between innovative activities and SMEs' performance.

Review of SME Policy on Innovation

- Legal framework
 - Law on MSMEs; Law on Sciences and Technology
- Strategic Action Plan for 2016-2020 and 2021-2025
- However, incentives regime for innovative activities in SMEs is not sufficient.

Review of SME Policy on Innovation

ASEAN SME Policy Index – Dimension 1: Productivity, Technology and Innovation

Technology and innovation promotion				
Country	Planning and design	Implementation	M&E	Total score
BRN	2.42	3.05	1.66	2.55
KHM	3.22	1.92	1.66	2.33
IDN	4.34	4.49	2.32	4.00
LAO	2.89	2.20	1.33	2.27
MYS	4.86	5.19	3.64	4.77
MMR	1.83	1.86	1.00	1.68
PHL	3.89	4.13	3.31	3.88
SGP	6.00	6.00	6.00	6.00
THA	5.56	5.05	3.98	5.01
VNM	3.70	4.07	1.99	3.52

Source: Report on ASEAN SME Policy Index 2018

Methodology and Data

- Probit model to estimate the factors affecting innovation
- $INNO_{it} = \gamma_i Z_{it} + \varepsilon_{it}$
- Where $INNO = 1$ if a firm introduces a new product or a new process or spends on R&D, and $= 0$ for otherwise.
- Z denotes a vector of a firm's characteristics, including size, foreign ownership, exporter,
- i, t denote an individual firm and time.

Methodology and Data

- Regression model to estimate the relationship between innovation and firm performance
- $sale_{it} = \beta_i INNO_{it} + \gamma_i Z_{it} + \varepsilon_{it}$
- The study utilizes the data from the World Bank Enterprise Survey (WBES) for Lao PDR in 2018

Descriptive analysis

New products/services			
introduced over last 3 years			%
Small	23	181	12.7%
Medium	21	61	34.4%
Large	9	23	39.1%

Introduced new/improved process			
over last 3 years			%
Small	28	181	15.5%
Medium	15	61	24.6%
Large	11	23	47.8%

Spent on R&D			
over last 3 years			%
Small	3	181	1.7%
Medium	3	61	4.9%
Large	2	23	8.7%

Estimation Results

Factors affecting product innovation

Variable	Dy/dx	P-value
Size	0.133	0.93
Foreign ownership	0.1331	0.03*
Exporter	0.0917	0.08

Estimation Results

Factors affecting process innovation

Variable	Dy/dx	P-value
Size	0.12	0.45
Foreign ownership	0.10	0.32
Exporter	0.19	0.28

Estimation Results

Factors affecting R&D

Variable	Dy/dx	P-value
Size	0.45	0.76
Foreign ownership	0.25	0.10
Exporter	0.49	0.34

Estimation Results

Relationship between innovation and sales performance

Variable	P-value
inno_product	0.013*
Inno_process	0.566
Inno_r&d	0.783

Conclusion and Policy Recommendation

- SMEs in general, particularly small-size have relatively low for innovative activities compared to the medium and the large.
- The study suggests that the foreign ownership affects the innovation, particularly product innovation.
- The study suggests that the SMEs that the positive effect on firm performance mainly comes from the improvement of existing products, an important type of innovation in SMEs.
- Regarding policy related to promote innovative activities in SMEs, the incentives regime; for example tax deduction, tax credit, should be in place.