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RESEARCH ARTICLE

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Abstract

This paper explores the current condition of the small and medium enterprises in Kazakhstan and their competitiveness. Theories of competitive advantage have been discussed and the data obtained from the Agency of Statistics of the Republic of Kazakhstan, The World Bank and the “Fund Damu” joint stock company surveys related to Kazakhstani small and medium enterprises were analyzed. It was found that Kazakhstani small and medium enterprises are mostly concentrated in the trading sector and small and medium enterprises’ structure of developed countries such as United Kingdom and Denmark is more diversified than in Kazakhstan. In addition, it was determined that contribution of Kazakhstani small and medium enterprises to gross domestic product of the country is very low compared with high income countries. Analysis of the sources of competitive pressure showed that most Kazakhstani enterprises do not experience high pressure from foreign competitors. The weakest identified indicators in Kazakhstani small and medium enterprises development are low rate of real annual sale growth, low share of companies obtained international certification, low share of companies using websites, low percentage of companies investing in research and development activities. As the main obstacles of running business-high tax rates, corruption and access to finance were determined. The suggestions for raising the level of competitiveness of Kazakhstani small and medium enterprises were provided in the conclusion of this article.

Keywords

competitive advantage • SMEs • entrepreneurship • strategies • strategic management power stations

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Nowadays, the issues of small and medium enterprises (SMEs) competitiveness attracts special attention of the governments worldwide because SMEs strongly affect employment rate, substantially contribute to gross domestic product (GDP), export volume and overall health of the economy in any country. In addition, SMEs and entrepreneurship are considered to be the forces of innovation and development. Kazakhstan also considers the SMEs development as one of its key success factors. As it was stated by the President of Kazakhstan, in order to increase the competitiveness of the national economy, the country has to increase competitiveness of Kazakhstani enterprises. Therefore, this problem is one of the most relevant and hot issues not only in the business world, but also in the scientific, political communities of contemporary Kazakhstan. High competitive Kazakhstani enterprises are the key to the success of Kazakhstan.

Currently, the government of the Republic of Kazakhstan administered various measures to support SMEs. By the government decree the “Fund Damu” joint stock company (JSC) was established. One of the main objectives of this fund is to support small and medium entrepreneurship. The fund supports entrepreneurs in the following ways:

- Direct financing of small enterprises involved in prioritized sectors of the economy.
- Financing companies to diversify small businesses
- Developing financial lease;
- Developing of microcredit organization networks;
- Developing the guaranty system of small enterprises’ obligations regarding second tire banks

Providing consulting services to small businesses in accordance with the programs developed by the Fund.

Kazakhstani SMEs are already competing at the world arena. Competition is expected to become more intense because Kazakhstan is planning to enter the World Trade Organization (WTO). In order to become competitive and survive these enterprises have to understand the forces underlying market competition. They have to follow best business management practices, produce high quality goods and services that meet international standards and benefit from the membership of WTO

by competing successfully in the world arena. Without deliberate preparation and understanding of market competitive forces some segments of Kazakhstani SMEs might be destroyed by the intense global competition.

Definition of the target problem for the analysis

The main purpose of the research is to analyze current situation and productivity of Kazakhstani SMEs Kazakhstan, identify existing problems in SME sector and provide suggestions for raising the level of competitiveness of Kazakhstani SMEs.

The review of literature on the problem

One of the most cited authors researching this problem is Michael E. Porter, the professor of Harvard Business School. According to Porter [10] competitive advantage stems from the value a firm might provide for its customers that exceeds the cost of its creation. Value here is determined as the price the customer is willing to pay. The author divides the competitive advantage mainly by two types: cost leadership and differentiation. The first type of competitive advantage occurs because companies are able to provide lower costs for goods or services and with equal benefits than competitors do. The second type is related to the unique benefits that are valued more than higher prices by buyers.

Kotler and Armstrong [5] consider competitive strategies as strategies that provide opportunity for organization to take competitive positions and provide it with sustainable competitive advantage. They define competitive advantage as advantage arising from products and services that better satisfy needs of target segments than products and services of competitors due to provision of more consumer value and lower prices for corresponding products.

Zimmerer et al. [15] emphasize the importance of competitive strategies for SMEs and define competitive advantage as collection of factors that distinguish SME from their competitors and provide it with unique market position to overcome its competitors. According to Zimmerer, from strategic perspective, the key to success is developing a unique advantage that create value for clients and difficult to duplicate. The company that has competitive advantage becomes a leader in the market and gains income above the industry average.

Theoretical frameworks considering competitive advantage include resource based view (RBV). A founder of the resource bases view is Penrose [9]. She described the firm as a collection of resources and stated that heterogeneity of services arising from resources provides each firm its uniqueness. Wernerfelt [13] determines resources as tangible and non-tangible assets that firms possess in the long term and stated that theory of competitive advantage might be build based on resources controlled by the firm.

Barney [1] has the following assumptions about RBV: 1) resources and capabilities that are valuable and rare provide

competitive advantage 2) resources that do not have substitutes and that cannot be duplicated generate sustainable competitive advantage.

Mahoney and Pandian [8], provide a counterargument for theory mentioned above. They state that mere presence of resources does not guarantee competitive advantage. The most important is how a firm uses its resources. Barney [1] also argued that the firm shall be administered in terms of structure, control system, rewarding policy, to fully exploit its resources.

Other views on the theory of competitive advantage are considered in the works of Michael Porter [10]. He states that the main instrument used for identification and sustaining competitive advantage is value chain. A value chain divides the firm into various activity types that it performs in production, design, and marketing and distribution of its goods and services. There are two main important issues that underlie competitive advantage. The first issue is industry attractiveness. Not all industries offer equal opportunities of stable profitability. The other important issue is determinants of relative position in the industry. In the same industries one firms are profitable than others and this does not depend on average industry profitability.

The critique for the Porter's theory is provided in the work of professor of Northern Kentucky University Datta [2]. First, the author discusses the Porter's cost leadership strategy. He supported the view that market share leaders more often follow differentiation strategy. As an example he cites General Motors as an example. This company was considered as a follower of cost leadership by the Porter. Datta [2] states that the company did not merely follow cost leadership strategy that caused its success; differentiation was also one of the success factors of this firm. A further critique on cost leadership is that this strategy is concerned with internal setting of the firm and does not focus on customers.

Datta [2] lists various researches whose arguments contradict with Porter's theoretical framework. First, he mentions Thompson and Strickland who offer "best cost provider strategy". This is the hybrid version that is in the middle between differentiation and cost leadership strategy. The car manufacturing company Lexus might be an example. When Toyota launched Lexus project, it used "best cost provider strategy". The price of Lexus was substantially below Germany's luxury cars. Second, he mentions Habrick who argued that cost leadership strategies are less profitable than differentiation strategies. This is because the firms that gained substantial market share usually compete following differentiation strategies rather than low costs strategies. Other authors mentioned by Datta [2] are Peters and Waterman who stated that companies showing high results consider more customer value rather than cost reduction. These companies prefer to stay close to customers. Datta [2] is convinced that differentiation is compatible with large market share and reduced costs and that higher quality may lead to lower cost.

We do agree with some arguments of Datta Companies that follow pure cost leadership strategies have big risk associated with falling behind those companies that are brave enough to spend a lot on research and development. Furthermore, we also support the idea that there might be a middle ground between differentiation and cost leadership strategies. In our opinion some companies might use cost leadership strategy and do not lose the opportunity for obtaining differentiation advantage.

Presentation of the research material

The analysis of the data provided by the Agency of statistics of the Republic of Kazakhstan shows that Kazakhstani SME's are concentrated in the industry of Wholesale and retail trade; repairing motor vehicles and motorcycles. 41% of all Kazakhstani SMEs are registered in this sector. Agriculture, fishing and forestry is another sector where majority of Kazakhstani enterprises are concentrated. As many as 22% of all Kazakhstani SMEs are involved in this industry. The third place is financing and insurance activities comprises 9%. We also analyzed number of SMEs by sectors in developed countries such as Denmark and UK in comparison with Kazakhstani statistics. Overall wholesale and retail trade prevail in SMEs of these countries. Probably, because it is simpler for SMEs to conduct business in this sector. This sector does not require entities to be very innovative, and make heavy investments in plant and

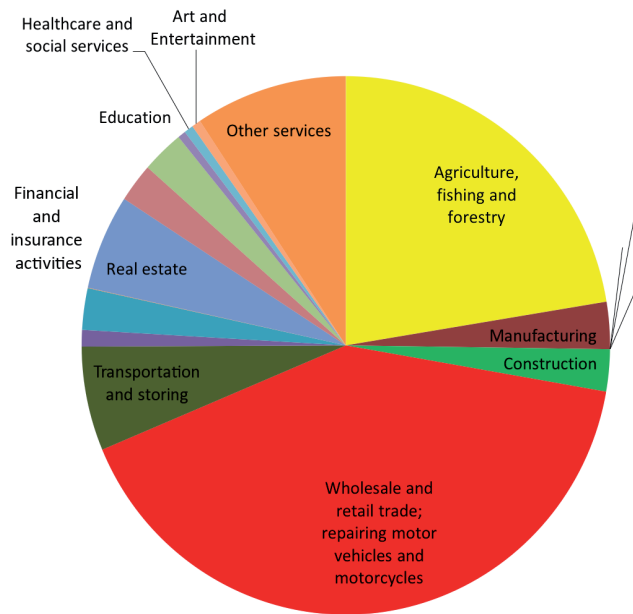


Fig. 1. Registered, active SMEs of the RK as at 1 quarter of 2013.

Source: http://www.stat.kz/digital/mal_pred/Pages/default.aspx [11]

equipment, the operating cycle is shorter; therefore the owners will have less problems with liquidity of their enterprises.

Figure 2 shows the number of active SMEs of Kazakhstan by sectors in comparison with SMEs of UK and Denmark.

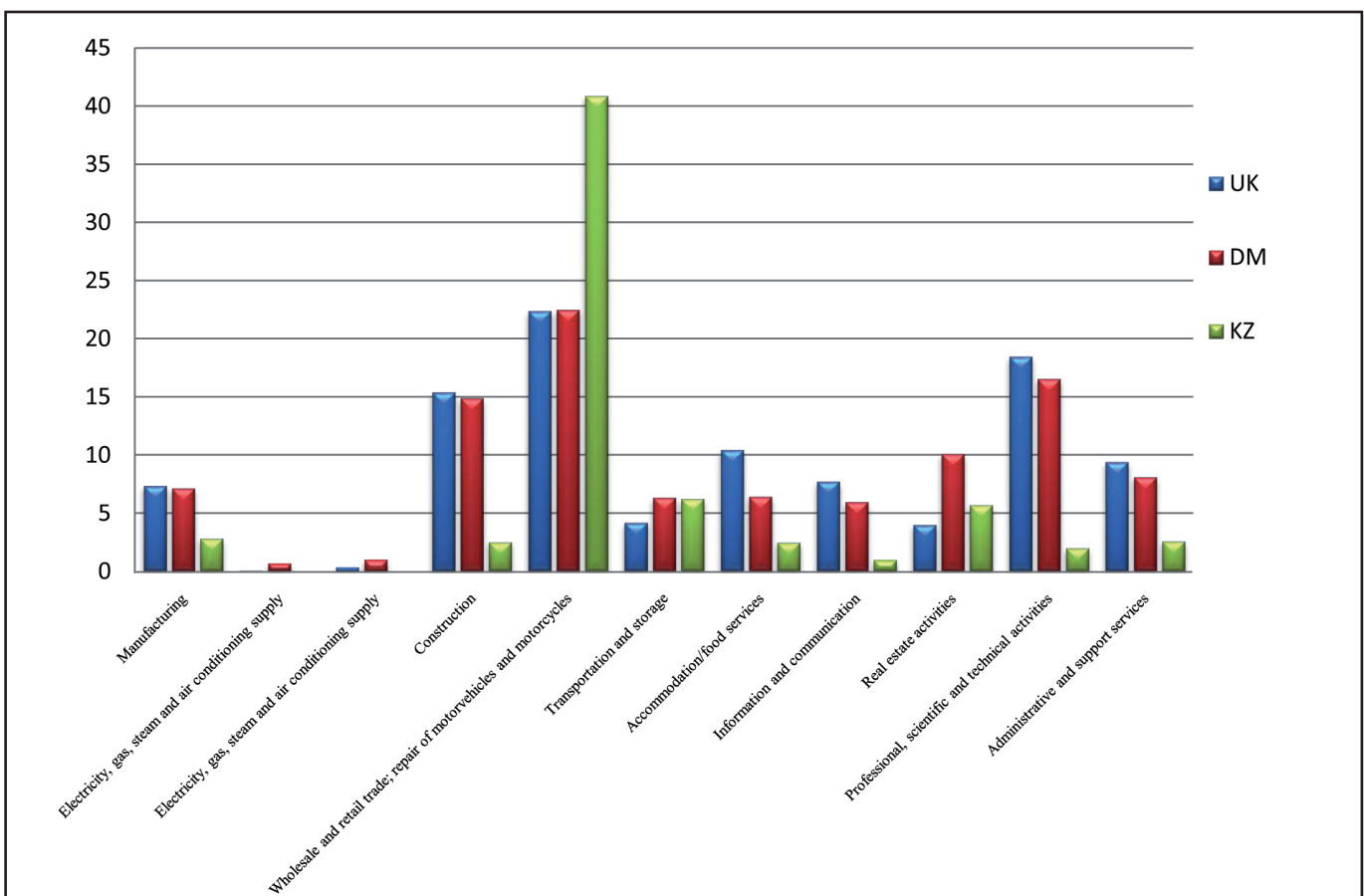


Fig. 2. Number of active SMEs by sector. Source: http://www.stat.kz/digital/mal_pred/Pages/default.aspx [11]

This picture indicates that SMEs of UK and DM are more diversified. Their SMEs succeeded in such sectors as construction industry, professional, scientific and technical activities. Furthermore some SMEs involved in waste management and remediation activities and this cannot be observed in the development of Kazakhstani SMEs.

Contribution of Kazakhstani Enterprises to GDP

According to the data of the World Bank, the contribution to GDP by SME varies from 16% in low income countries, 30% in medium income countries, to 51% obtained in high income ones. Typically in the low income countries the sector of SMEs is large, but informal. Figure 3 shows the dynamics of contributions made by Kazakhstani SMEs to the GDP of the Republic of Kazakhstan. During 2011 SMEs contributed approximately 17,5% that is close to those in low income countries. The maximum share of contribution was made in 2009 and comprises approximately 20,5%.

Major obstacles for business development

The World Bank conducted a survey of 544 companies by meeting with their owners and top managers. Figure 4 shows the sizes in terms of number of employees and sectors of the firms surveyed. The majority of the companies (70% or 380 entities) were small and medium enterprises. In the division by sectors service and manufacturing firms prevail.

The summary of findings presented by the World Bank are provided in Figure 5 that identifies the main barriers for conducting business in Kazakhstan.

The most important problem for conducting business as reported by Kazakhstani enterprises is high tax rates. As many as 46.4% of small business enterprises and 44.4% of medium enterprises recognized high tax rates as the main business constraint. Small and some medium entities in Kazakhstan use special tax regimes that require paying entities only 3% of object of taxation (which is quarterly declared income). Entities that use general tax regime pay 20% of corporate income tax (CIT) as the share of aggregate annual income after deductions and adjustments. As Reported by KPMG, the average global CIT rate was 25.38%, Asian average was 25.73% and EU's average CIT rate was 23.22% in 2009. In developed countries such as USA and UK the CIT tax rates are 40% and 28% accordingly [6]. Value added tax rate in Kazakhstan is 12% while in Asia it is 11,8%, average in EU countries is 19.52% and global average was 15.39% in 2009 [7]. Therefore, it might be concluded that the problem of high tax rates is exaggerated by Kazakhstani SMEs.

The second most important constraint of running business in Kazakhstan is corruption. As it was determined, based on the World Bank, 15.2% of all surveyed business companies reported corruption as the main barrier for running their business. "Percent of firms expected to give gifts to secure government

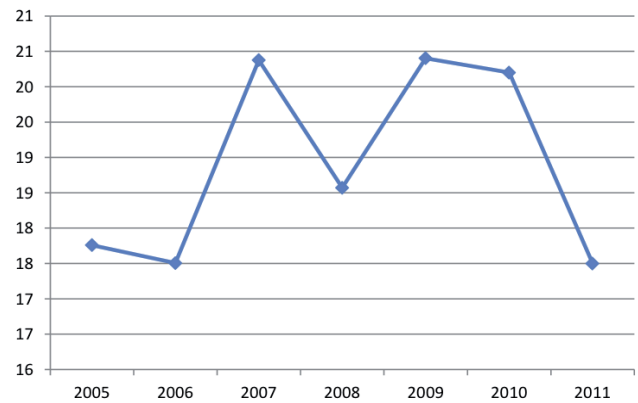


Fig. 3. Dynamics of contribution to GDP by SMEs of the Republic of Kazakhstan. Source: http://www.stat.kz/digital/mal_pred/Pages/default.aspx

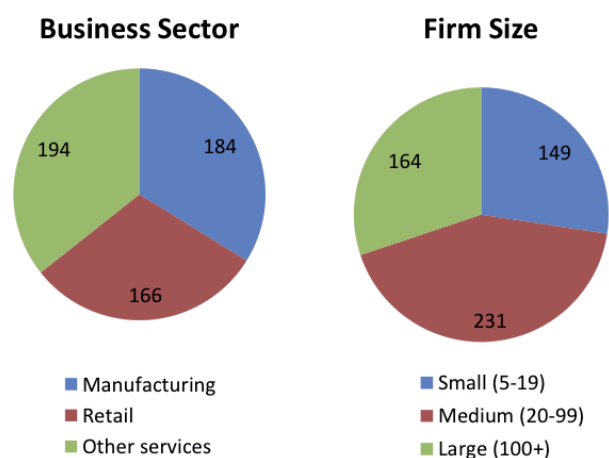


Fig. 4. Surveyed firm sizes and business sectors.

Source: <http://www.enterprisesurveys.org> [14]

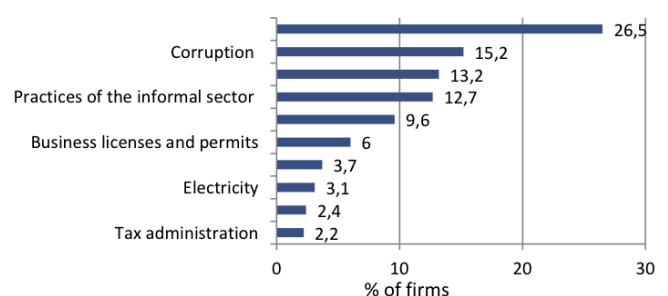


Fig. 5. Top ten business constraints for firms in Kazakhstan in 2009.

Source: <http://www.enterprisesurveys.org> [14]

contracts" in medium business comprised 64,5% and 10% in small businesses". Furthermore, "the percent of firms expected to give gifts to public officials "to get things done" comprised 30% in small businesses, while in large business was 36%.

The third biggest problem comprising 13.2% of all respondents is ability of companies to access financing. Generally, the

unsecure loans rates of Kazakhstani banks are very high ranging from 16% up to 30%. Currently, the government provides subsidized loans to SMEs. If an SME is able to secure 36% of the amount of the loan by its capital, it might obtain the 7% loan from the second-tire banks. However, obtaining such loan is a very complicated procedure. First, SMEs have to obtain approval from the bank and then their application shall be considered by city administration. This probably influences the level of corruption because final decision for financing is made by the city administration.

How competitive Kazakhstani companies are?

The Figure 6 shows the share of companies that were awarded international quality assurance certification. Compared with other countries the share of Kazakhstani companies that obtained international quality assurance certification is very low. In comparison with China and Malaysia, this share is five times lower. According to the research data only 4.7% of small and 10.8% of medium business reported possession of international quality assurance certification. In China and Malaysia this indicator comprised 54% and 53.4% accordingly.

Another problem identified from the analysis of World Bank data is real annual sale growth rate of Kazakhstani SMEs. In 2009, the real annual sales growth of small business was negative comprising -3.1% and for medium business 1.9%. On the average this indicator in Eastern Europe and Central Asia countries comprised 5.4% for small business and 7% for medium businesses.

In Figure 7 it might be observed that overall growth of sales of Kazakhstani enterprises comprised only 0.3%. This is a very weak indicator. Leading country in the Eastern Europe and Central Asia region by this indicator is Armenia. Its sale growth comprised 19.4% that is almost twenty times larger than in Kazakhstan.

To evaluate the innovativeness of Kazakhstani enterprises, the quantity of Kazakhstani entities that developed websites were identified. The analysis showed that the share of companies that have their own websites comprised 26.5%. This is relatively low indicator because on the average, share of use of internet by the companies located in the Eastern Europe & Central Asia region comprised 49%.

Furthermore, we have found that the share of Kazakhstani SMEs that invest in research and development (R&D) comprise only 10%. Statistics of World Bank indicate that among 380 SMEs, 38 companies responded that they invested in research and development activities. This is a relatively weak indicator in comparison with other countries located in the Central Asia and Eastern Europe region. Generally, this indicator ranges from 10 to 32% in the region, except Uzbekistan. In Uzbekistan only 2% of all interviewed 200 SMEs declared investment in R&D. Nearest neighbor of Kazakhstan–Russia, reported 30% involvement of its SMEs in R&D activities (when interviewed,

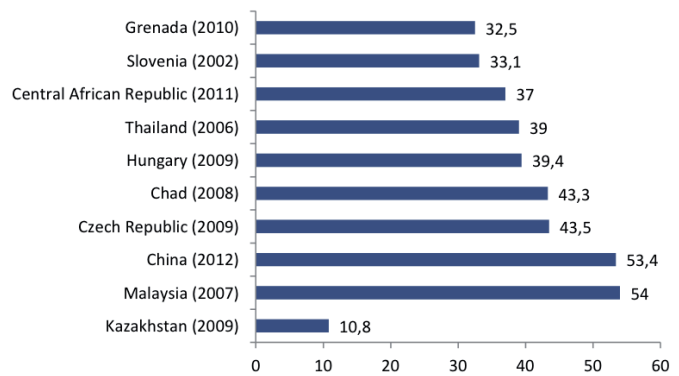


Fig. 6. The percentage of companies obtained international quality assurance certification.

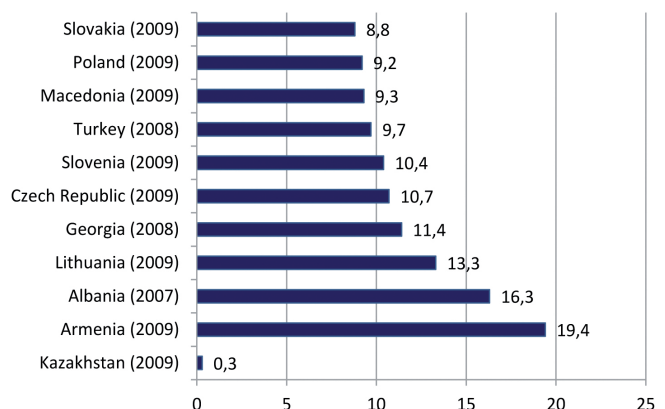


Fig. 7. % Real annual sale growth. Source: <http://www.enterprisesurveys.org> [14].

as many as 254 out of 769 Russian SMEs reported that they had invested in R&D activities).

The share of interviewed 380 SMEs that introduced new products or services in the last 3 years comprised 42% (162 out of 380 companies declared the introduction of new products by their organizations). In Russia this coefficient comprised 65% and in Armenia 60%. (196 out of 326 Armenia's SMEs reported that they introduced new products or services in the last 3 years). In Uzbekistan this indicator comprised 25%. Out of 200 companies, only 49 confirmed the introduction of new products in last three years.

Competitive pressure

Table 1 shows the sources of competitive pressure on Kazakhstani SMEs. Sample of 380 responses of SMEs owners and managers were analyzed. First, the pressure to develop new products was analyzed. It was identified that the biggest pressure comes from domestic competitors. As many as 58% (34% very important and 24% fairly important) of all respondents think that the pressure to develop new products originates from domestic competitors. Furthermore, it was determined that the

Tab. 1. Perception of pressure on Kazakhstani SMEs on development of new products. Source: <http://www.enterprisesurveys.org> [14].

	Effect	Don't know	Fairly important	Slightly important	Very important	Not at all important
1	Effect on decisions to develop new products: pressure from domestic competitors	6	129	93	90	62
	%	2	34	24	24	16
2	Effect on decisions to develop new products: pressure from foreign competitors	18	55	62	24	224
	%	5	14	16	6	59
3	Effect on decisions to develop new products: pressure from customers	7	107	91	70	105
	%	2	28	24	18	28

Tab. 2. Perception of pressure on Kazakhstani SMEs on production costs. Source: <http://www.enterprisesurveys.org> [14].

	Effect	Don't know	Fairly important	Slightly important	Very important	Not at all important
1	Effect on decisions on production costs: pressure from domestic competitors	15	128	90	80	67
	%	4	34	24	21	18
2	Effect on decisions on production costs: pressure from foreign competitors	21	43	64	24	227
	%	6	11	17	6	60
3	Effect on decisions on production costs: pressure from customers	18	98	101	57	107
	%	5	26	27	15	28

pressure to develop new products from customers is also substantial. Forty six percent of all respondents (28% fairly important and 18% important) percept the pressure from customers to develop new products. On the other hand the table shows that only 20% respondents feel pressure from foreign competitors in terms of new product development.

Table 2 analyzes the forces affecting the production costs of Kazakhstani SMEs. As in the case with new product development, Kazakhstani SMEs percept pressure mostly from domestic competitors. 55% (34 fairly important and 21% very important) of all respondents think that their decision regarding costs is mainly affected by domestic competitors. Pressure from customers is perceived by 41% and pressure from foreign competitors is declared by only 17% of all respondents.

Needs of Kazakhstani entrepreneurs

To identify the main needs of Kazakhstani entrepreneurs "Fund Damu" JSC conducted a survey with participation of entrepreneurs and people who were planning to establish their own business. As many as 3877 participants were asked to identify the types of support to be provided by "Fund Damu" JSC. The

results of this survey are presented in the Table 3. According to this table, the main needs of entrepreneurs are related to access to finance. The largest share 29% of all respondents stated that they wish to be provided with grants for their start-up projects. The next largest portion of respondents (604 people or 16%) declared that they are interested in obtaining loans from "The Damu Program" with low interest rates. Further, 452 respondents or 12% of people in the sample responded that they wish to be provided with subsidized loan of "Damu Start Up" program.

The survey also identifies other factors important for business development. These factors include free courses teaching basics of how to run business, availability of marketing research data, availability of completed business plans, and the opportunities to cooperate and network with foreign enterprises.

Conclusions and further studies prospective;

The statistical data of SMEs across sectors showed that most of the Kazakhstani SMEs involved in whole and retail trade, repairing motor vehicles and motorcycles. Their share comprised 41%. The analysis of the statistical data of SMEs of developed countries indicated more diversified structure. According to

Toxonova [12], the Vice President of Economic Research Institute, the reasons for involvement of SMEs in the trading sector are guaranteed short pay-back period in trade (the payback period of investments into trade makes from 0.5 to 1 year, in manufacturing 3-10 years):

- High Start-up capital requirements in manufacturing
- lack of owners equity;
- high level of investment risks associated with starting manufacturing company.

Another problem identified in this research is low contribution of Kazakhstani SMEs to the GDP of the country. In our opinion this is because there are a lot of informal enterprises in Kazakhstan. Government has already taken measures to simplify tax regime for SME and reduced tax burdens on this entities. However, there are still a lot of problems associated with official registration of SMEs. By being officially registered SMEs become vulnerable to unnecessary requirements of numerous government bodies. The government bodies intentionally create obstacles and interpret the laws to their favor. This is supported by the survey data of the World Bank. Corruption is identified as the second most important constraint of running business in Kazakhstan.

Further obstacles of running business in Kazakhstan were high tax rates and access to finance. From the comparative analysis it is determined that Kazakhstani enterprises exaggerate the problem of high tax rates. Comparing to international tax rates analyzed by KPMG, the tax rates in Kazakhstan are not very high. On the other hand, the problem of access of entrepreneurs to finance remains very relevant. According to the World Bank survey, this is the third main obstacle of running business in Kazakhstan. It is also confirmed by the survey conducted by "Fund Damu" where most of the respondents determined that the access to financing is the most important issue in business development.

The main weak areas identified by the analysis of World Bank data are low rate of real annual sale growth, low share of companies obtained international certification, low share of companies using websites, low percentage of companies investing in research and development activities.

What might be done?

The problem of intense trading sector in Kazakhstan might be an opportunity for Kazakhstani SMEs. Trading for companies in Kazakhstan provided very valuable experience because they are already familiar with local market demands and distribution channels (down-stream side of business). Those trading firms might gradually be transferred to manufacturing sector and other sectors and this could be their growth strategies.

Tab. 3. Assessment of entrepreneurial needs.

Source: <http://www.damu.kz/> [4].

	Needs	% of respondents	Number of respondents
1	Free courses for beginning entrepreneurs	14.39	558
2	Free completed and detailed business plan / Marketing research findings	8.18	317
3	Free courses for existing entrepreneurs (advanced entrepreneurial courses)	2.35	91
4	Free consulting and business support services for existing businesses	1.88	73
5	Free business courses teaching top	3.46	134

Experience of various successful international companies show that most of them have unique and valued proposition for the market and know how to control and minimize costs. These companies have competitive advantage because their goods more valued by customers or their prices are lower than prices of their competitors (quality being equal), or they have both cost advantage and differentiation advantage over their rivals. Therefore, companies in Kazakhstan might follow these strategies.

As an instrument for achieving success SMEs in Kazakhstan shall use value chain analysis. Following the strategies developed by Porter they have to divide their companies into value chains to identify the areas for improvement.

Those Kazakhstani SMEs that are already succeeding shall identify and cherish those resources that give them opportunity to be unique to sustain their competitive advantage. They have to remember that only with proper management and rare and valuable resources those SMEs might remain competitive and face new challenges.

Finally, Kazakhstani SMEs shall try to be more innovative. First, Kazakhstani companies shall be guided by international standards and certification. Kazakhstani SMEs also have to increase the usage of internet in their activities and perceive its importance. In addition, the share of SMEs investing in R&D activities shall be increased. Of course it is very costly and risky for companies to invest in research and development activities; however, Kazakhstani SMEs should also remember that new product development provides great opportunities for their growth and competitiveness.

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