

## Globalization, Inclusion, and E-Commerce: Agenda for SMEs

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Globalization created wealth and improved standards of living and promoted convergence of incomes across economies. Yet, globalization's benefits have been seen as heavily tilted towards multinational corporations (MNCs). It is perceived that this was enabled by the rules of global trade which are stacked against small and medium-sized enterprises (SMEs). Today's global agenda on greater inclusion is meant to remedy the disadvantages faced by small firms.

Eighty percent of global trade takes place through global supply chains.<sup>2</sup> This explains policymakers' interest in finding ways to facilitate SMEs' access to GVCs. However, stringent industry standards at each step of the value chain and burdensome certification processes impede SMEs' participation in GVCs.<sup>3</sup> Multinationals, for their

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<sup>2</sup> UNCTAD. Global Value Chains and Development – Investment and Value Added Trade in the Global Economy. Geneva: UNCTAD. (2013), Available at: [http://unctad.org/en/PublicationsLibrary/diae2013d1\\_en.pdf](http://unctad.org/en/PublicationsLibrary/diae2013d1_en.pdf).

<sup>3</sup> See, for example, the collection of APEC PSU case studies on manufacturing-related services (<https://www.apec.org/Publications/2015/11/Services-in-Global-Value-Chains-Manufacturing-Related-Services>).

part, are strict about onboarding suppliers because they are as fragile and prone to failure as their weakest supplier.<sup>4</sup> In many developing economies where capital for upgrading technology and equipment is lacking, SMEs find substantial participation in MNCs' operations beyond reach.<sup>5</sup>

This policy brief considers an alternative route to SME internationalization through e-commerce. While SMEs face a different challenge of access with e-commerce, most of it can be abated through regulatory facilitation.

## **E-commerce and SME Globalization**

### *E-commerce supports SMEs' participation in international trade*

The Internet has empowered SMEs to sell to a bigger market. Success stories abound of simple entrepreneurs growing their business and succeeding in the export market. Most start with selling to a bigger set of 'friends' through Facebook or Snapchat, which is usually the easiest way for entrepreneurs to get an online selling experience. In time, successful SMEs get discovered and connected with e-commerce marketplace platforms that open up a much bigger market for SMEs' products. For example, the shoe business of Malaysia's Christy Ng began humbly in her mother's garage. She started selling by posting unique designs of shoes on Facebook which gained her thousands of fans within the first month. The positive response and growth in demand led to the creation of a blog with shopping cart plugins, and, eventually, to an online store on eBay which showed her products to major international markets. Today, Ng's e-commerce store is complemented by physical shops in 5 different locations in Malaysia, a far cry from the 'garage' business it started from.

With e-commerce, SMEs can, in theory, establish an instant global presence by simply setting up a website. In practice, it is not as simple because there are a host of regulations including privacy standards and security safeguards to comply with, especially if its website includes a shopping cart plug-in. There are, however, other avenues for SMEs to sell online. One is through a simple Facebook page or participation in other similar social networking sites. Another is by joining platform-based e-commerce sites such as Amazon, eBay, Alibaba, or even domestic- or region-based e-commerce platforms like Lazada, Lelong, and many others.

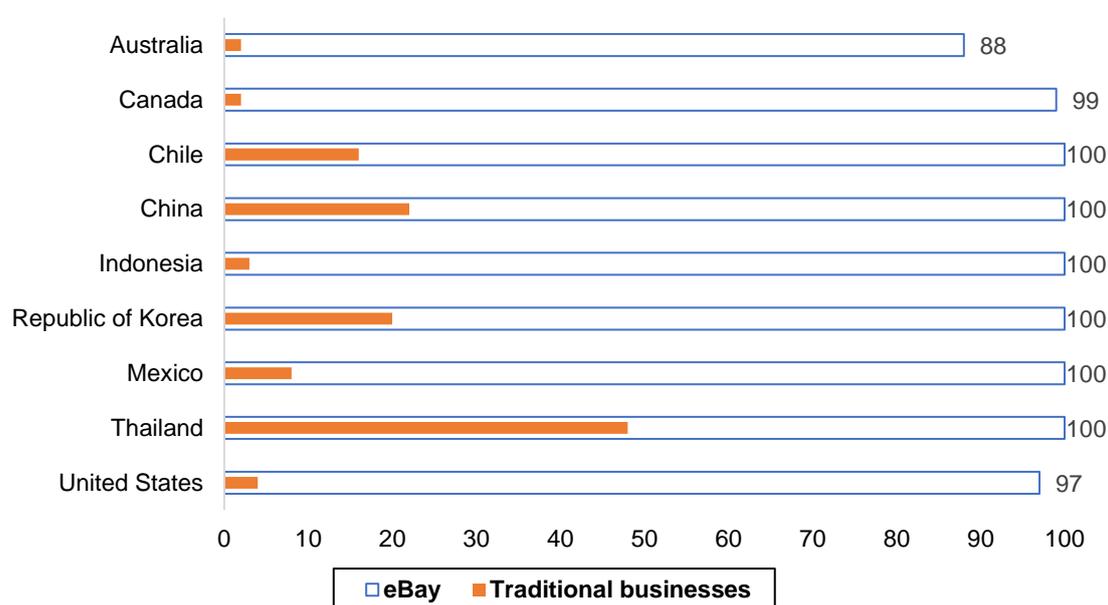
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<sup>4</sup> Nicita, A., V. Ognitsev and M. Shirotori. Global Supply Chains: Trade and Economic Policies for Developing Countries. New York and Geneva: UNCTAD. (2013), Available at: [http://unctad.org/en/PublicationsLibrary/itcdtab56\\_en.pdf](http://unctad.org/en/PublicationsLibrary/itcdtab56_en.pdf).

<sup>5</sup> A PSU study, for example, found that big multinationals tend to find domestic SMEs incapable of meeting their product demands, hence tend to work with and encourage their own supply network from home economy to co-locate with them when they move production to another economy (see the case studies on manufacturing of aircraft control systems and car in the Philippines <https://www.apec.org/Publications/2015/11/Services-in-Global-Value-Chains-Manufacturing-Related-Services>).

A study by eBay Public Policy Lab,<sup>6</sup> drawing on data of its own registered sellers, supports the observation that e-commerce enables SME participation in the global market. Figure 1 shows that almost all of eBay's registered online sellers in selected economies are able to export globally, compared to a relatively small percentage of SMEs in traditional (offline) business. In addition, SMEs that sell online are able to reach more markets than those in traditional business. On average, firms are able to reach an average of 30 different economies using platforms for e-commerce.<sup>7</sup> Additionally, 74 per cent of these SMEs are still exporting after three years in contrast to 15 per cent of those engaged in offline export.<sup>8</sup>

**Figure 1. Share of exporters in eBay vs. traditional businesses (in percentage)**



Note: The eBay data reflects the share of 2014 eBay Commercial Sellers (those with \$10,000 USD or more in sales on eBay) in each economy, who exported in that year.

Source: eBay (2016)

### *Expanding opportunities for SMEs from e-commerce*

More SMEs can benefit from the expected growth in online consumer demand in the coming years. Forecast by eMarketer made in 2015 indicated that retail e-commerce

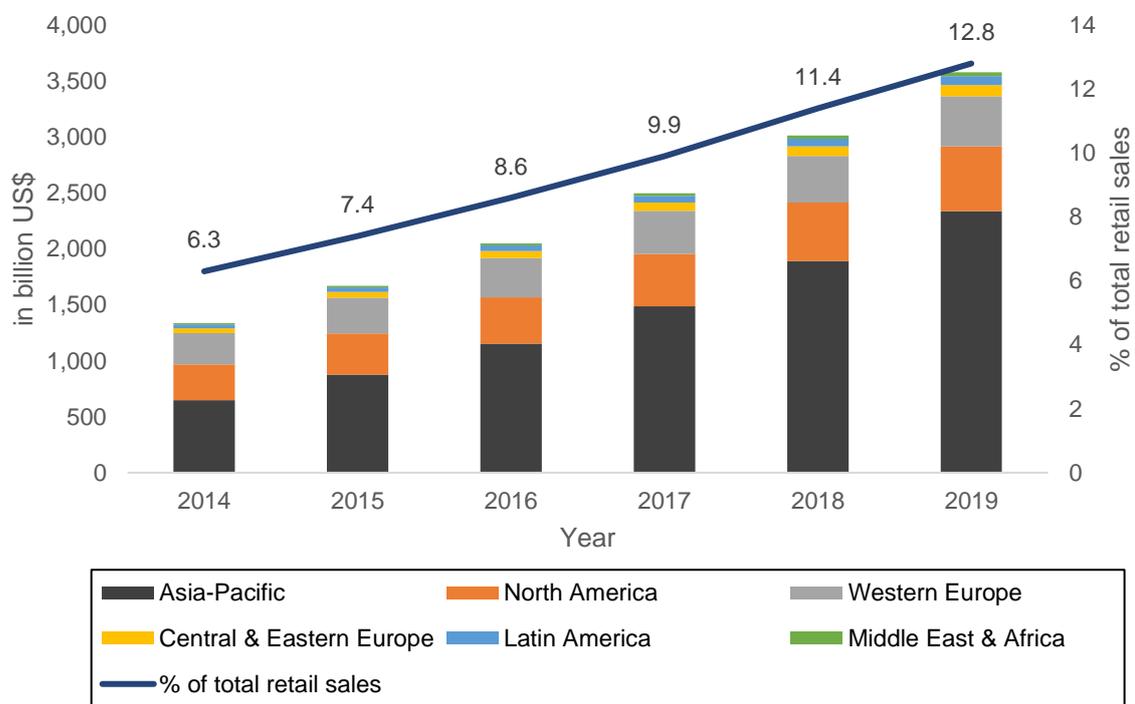
<sup>6</sup> eBay. Small Online Business Growth Report. San Jose: eBay. (2016), Available at: [https://www.ebaymainstreet.com/sites/default/files/ebay\\_global-report\\_2016-4\\_0.pdf](https://www.ebaymainstreet.com/sites/default/files/ebay_global-report_2016-4_0.pdf).

<sup>7</sup> Olbe, H.M. Bridging Distance for Development: Regulatory Cooperation Applied to Consumer Rights, Parcel Delivery and Sales Tax. Washington D.C.: IDB and Geneva: ICTSD. (2017), Available at: <http://e15initiative.org/publications/bridging-distance-for-development-regulatory-cooperation-applied-to-consumer-rights-parcel-delivery-and-sales-tax/>.

<sup>8</sup> eBay. 2015 US Small Business Global Growth Report. San Jose: eBay. (2015), Available at: <https://www.ebaymainstreet.com/sites/default/files/2015-us-small-biz-global-growth-report.pdf>.

will increase from USD1.3 trillion in 2014 to USD3.6 trillion in 2019 (figure 2), and its share to total retail sales will more than double from 6.3 to 12.8 per cent between 2014 and 2019.<sup>9</sup> Asia-Pacific, North America and Latin America are collectively expected to increase its share of retail e-commerce sales to 85 per cent by 2019. While the online business-to-consumer (B2C) market is growing, its size is dwarfed by the business-to-business (B2B) market which, in 2015, stood at USD22.4 trillion. To date, most e-commerce transactions have been domestic, but cross-border retail e-commerce is anticipated to grow at twice the rate of domestic e-commerce until 2020.<sup>10</sup> This opens a potentially bigger market for SMEs if given the right regulatory and infrastructure support.

**Figure 2. Global retail e-commerce sales poised to grow**



Note: Retail e-commerce includes products or services ordered using the internet via any device, regardless of payment or fulfillment method. Excludes travel and event tickets.

Source: eMarketer (2015)

<sup>9</sup> eMarketer. Worldwide Retail Ecommerce Sales: eMarketer’s Updated Estimates and Forecast Through 2019. (2015), Available at: <https://www.scribd.com/document/321791802/EMarketer-2016-Worldwide-ECommerce-Report>.

<sup>10</sup> International Trade Centre (ITC). New Pathways to E-commerce – A Global MSME Competitiveness Survey. Geneva: ITC. (2017), Available at: [http://www.intracen.org/uploadedFiles/intracenorg/Content/Publications/New%20Pathways%20to%20E-commerce\\_Low%20res\(2\).pdf](http://www.intracen.org/uploadedFiles/intracenorg/Content/Publications/New%20Pathways%20to%20E-commerce_Low%20res(2).pdf).

## Supporting SMEs in E-commerce

Despite the inspiring stories of SMEs succeeding through e-commerce, the number is a mere drop in a bucket considering that SMEs number in the millions. We discuss below various challenges in supporting SME internationalization through e-commerce, gleaned from focused discussions and interviews with major stakeholders in e-commerce, including SMEs, technology-enabled marketplace platform operators, payment providers, aggregators, logistics providers and relevant government agencies.<sup>11</sup>

### 1. Raise awareness and build capacity

#### *Low SME participation*

Awareness among SMEs on how to participate and benefit from e-commerce is poor. For example, a survey conducted by the SME Corporation Malaysia in 3Q of 2016 showed that less than 26 per cent of SMEs are involved in selling products or services online. In the Republic of Korea, while 34 per cent of larger firms were engaged in e-commerce in 2013, only 15 per cent of SMEs did so.<sup>12</sup> Several reasons explain the relatively low participation by SMEs in many economies including poor connectivity and lack of awareness by many SMEs as well as fear of trying and misconceptions about e-commerce.

#### *SMEs should have a unique value proposition*

Salability of SMEs' products depends on attractive packaging, taste/preference in

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<sup>11</sup> This draws mainly from Pasadilla, G., A. Wirjo and J. Liu. Promoting E-commerce to Globalize MSMEs. Singapore: APEC Policy Support Unit. (2017), Available at: <https://www.apec.org/Publications/2017/11/Promoting-E-commerce-to-Globalize-MSMEs>. The focused group discussions and interviews with major stakeholders in e-commerce (e.g. SMEs, technology-enabled marketplace platform operators, payment providers, aggregators, logistics providers and relevant government agencies) took place in five economies: Brunei Darussalam, China, Korea, Malaysia, and Chinese Taipei. Other sources include: 1) Accenture. Cross-border Ecommerce. (2016), Available at: <https://www.scribd.com/document/332919657/Cross-Border-Ecommerce-Accenture>; 2) A.T. Kearney. Lifting the Barriers to E-Commerce in ASEAN. (2015), Available at: <https://www.atkearney.co.uk/documents/10192/5540871/Lifting+the+Barriers+to+E-Commerce+in+ASEAN.pdf/d977df60-3a86-42a6-8d19-1efd92010d52>; 3) Competition Commission of Singapore. Handbook on E-Commerce and Competition in ASEAN. (2017), Available at: [https://www.ccs.gov.sg/~media/custom/ccs/files/media%20and%20publications/publications/inhouse%20publication/ccs\\_e-commerce%20handbook\\_2017.ashx](https://www.ccs.gov.sg/~media/custom/ccs/files/media%20and%20publications/publications/inhouse%20publication/ccs_e-commerce%20handbook_2017.ashx); 4) eBay. Commerce 3.0: Enabling ASEAN Small and Medium Enterprises (SMEs). (2015), Available at: [https://www.ebaymainstreet.com/sites/default/files/asean\\_commerce\\_3\\_0\\_final\\_1.pdf](https://www.ebaymainstreet.com/sites/default/files/asean_commerce_3_0_final_1.pdf); 5) International Centre for Trade and Sustainable Development (ICTSD) and World Economic Forum (WEF). Maximizing the Opportunities of the Internet for International Trade. Geneva: ICTSD and WEF. (2016), Available at: [http://www3.weforum.org/docs/E15/WEF\\_Digital\\_Trade\\_report\\_2015\\_1401.pdf](http://www3.weforum.org/docs/E15/WEF_Digital_Trade_report_2015_1401.pdf); and 6) ITC (2017).

<sup>12</sup> Large firms in Korea are those with more than 250 employees, while SMEs are those with 10-49 employees.

target markets, and price. Not to be underestimated is the desirability of product information written or translated into the buyers' language if SMEs want to increase foreign sales. To succeed, SMEs need to be aware of and capitalize on the unique value proposition of their products. This is all the more important in e-commerce considering the competition intensity and product varieties that compete for buyers' attention online.

#### *Business fundamentals and technology skills upgrading*

Many SMEs are deficient in knowledge of business fundamentals required to go online. SMEs do not have complete knowledge of the different components of e-commerce (see figure 3 for examples) and corresponding cost. Consequently, SMEs do not always factor all the associated costs into the final product price leading to either a loss or only minimal profit.

Also critical is the technical know-how among SMEs. Basic computer skills are necessary to access account and check online orders among other things. Furthermore, in the digital world, buyers who cannot touch and examine products physically care a lot more about good product presentations, either in pictures or videos or written descriptions, as well as endorsements from other consumers. In addition, they need to understand consumer preferences and mentalities to choose, for example, the right keywords or ad words for their products, to increase their probability of surfacing in product searches.

#### *Knowing which platform is appropriate for their products*

There is a plethora of platforms that SMEs can join, starting with social networking sites. In fact, many usually start their online businesses through social media because it is costless to open an account there. They can also try the waters in social networking sites without the rigid requirements of platform-based e-commerce sites. Not all social media platforms, however, are the same. For example, Instagram is more popular among teenagers and youth, hence are appropriate for products targeted for the young. Yet, not all SMEs are savvy about making distinctions among different platforms.

#### *Platform regulations and scaling up difficulty*

Marketplace e-commerce platforms facilitate access to a wider market, and particularly in the case of cross-border trade, provide the necessary regulatory information collection needed to sell abroad. For SMEs joining marketplace platforms, however, adhering to its set terms and conditions may be challenging. Conditions can include requirements to use specific platform-accredited logistics providers; strict delivery timeline like shipping product out within 24 hours from order receipt; and

predetermined returns policy, often longer and more generous than the seller's own.

Adhering to platforms' policy entails that the SMEs should have grown sufficiently able to supply products with a minimum scale, a growing up problem that not all SMEs can successfully overcome. This entails not only additional capital investments but also investment in systems and technology to automate orders, keep track of inventories across platforms as well as respond efficiently to multiple customer enquiries.

### *Role for 'aggregators'*

Aggregators or intermediary firms help facilitate SMEs participation in e-commerce by acting as middlemen, sometimes with e-commerce platforms, or directly with importers abroad. They usually have a more extensive experience in cross-border e-commerce, as well as network relationships with logistics service providers than individual SMEs. They can also take care of all the necessary arrangements to participate in e-commerce including repackaging, pricing, and dealing with all the requirements by the technology platforms and from international markets, thereby enabling SMEs to focus on production activities.

## *2. Continue with efforts to improve business environment*

Finding out and dealing with various rules and regulations to set up and run businesses across economies is challenging for all firms, but especially for SMEs which have limited resources. Making this information more easily available is one way to help businesses; but fulfilling them is another matter. Sometimes, specific regulations impose obligations that essentially preclude SMEs' participation in the foreign e-commerce market. For example, regulations requiring listed sellers on domestic-based e-commerce platforms to be registered domestically effectively foreclose the chances of foreign SMEs to sell through that platform.

Interviews conducted with e-commerce stakeholders disclose the role that aggregators play in such situations. Unlike SMEs, aggregators have the necessary resources to register its business in multiple locations, and thus are able to export using different domestic e-commerce platforms. For example, a Korean aggregator can register as a Japanese and Chinese business in Japan and China respectively, list with Rakuten or Alibaba or Taobao, and thus be able to sell Korean products in the respective markets.

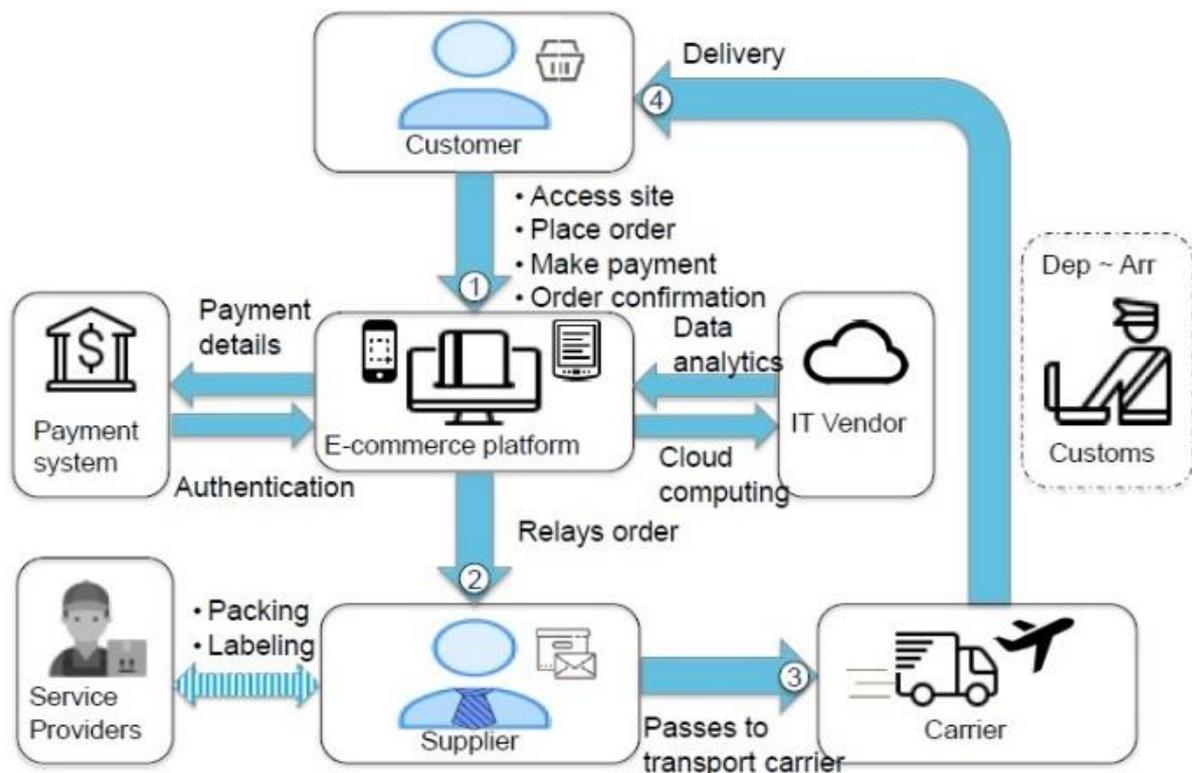
While governments' purported policy is to help SMEs, some regulations inadvertently do the opposite. For example, it is usual that small sellers run very tight operations and use their residences for production. However, in one ASEAN economy, SMEs cannot use a home address to apply for value-added tax (VAT) registration number; and without it, e-commerce platforms cannot register the small seller.

Other regulations that vary across economies add to the difficulties. For example, not all economies recognize e-contracts, making online contract fulfillment more burdensome and costly.

3. *Develop robust e-commerce ecosystem: Payments, fulfillment centers, logistics*

Seamless e-commerce experience necessitates that various actors in the e-commerce ecosystem, including secured payment system and shipping/logistics, work with minimal friction. Figure 3 illustrates a simple ecosystem which an online consumer interacts with but may be unaware of. Challenges in any components of the ecosystem will impact e-commerce and hence the market opportunities for SMEs.

**Figure 3. Simplified diagram of an e-commerce ecosystem**



Source: Adapted from Drew & Napier seminar presentation (2017)

*Payment services*

Payment services require correspondent banking relationships or agreements between banks, as well as between payment service providers and banks. However, discussions on such arrangements have become more tedious due to anti-money laundering and counter-terrorism financial laws in developed economies where majority of the payment service providers are headquartered. In some economies, the cost-benefit ratio for payment services providers does not work out, hence limiting the available payment options and consequently, sellers' possibilities to sell to foreign

markets where consumers prefer the unavailable payment options. Even if available, thinly-staffed SMEs find the onboarding process laborious and, in some cases, costly due to the required provision of reserves for chargebacks.<sup>13</sup> Other limitations include their inability to hedge their foreign exchange receipts because payment service providers dictate the exchange rates for the remittance of their earnings.

Low percentage of banked population also represents a challenge for e-commerce, although creative means and forms of payment including cash payments through a network of retail outlets or the use of mobile payments have been developed to overcome them.

### *Advertising and internet services*

Online sales rely on targeted advertising, which in turn depends on big data analysis of buyers' browsing behavior for example. Advertising can help raise shopping conversion rates,<sup>14</sup> unless the data analytics was based on fake traffic created by bots. In some economies, however, cross-border access to customer browsing data may be restrictive. Moreover, geo-blocking which prevents domestic buyers from viewing sites abroad also prevent SMEs from selling to a larger market.

On internet connectivity, high cost of access impedes SMEs' interest to use e-commerce, while poor connectivity frustrates potential buyers who are used to a fast response to customer clicks.

### *Logistics*

A compelling appeal of e-commerce for consumers is the convenience of having products delivered to their location of choice. SMEs, especially from developing economies, face a range of logistical challenges. They tend to face higher cost because of low sales and shipment volume between certain locations. For example, it is cheaper to ship goods across the Pacific or Atlantic, than within the ASEAN region. Cheaper domestic logistics providers may be available but they may not operate in a wide number of markets or have insufficient capacity for security and safety measures. Low frequency of cargo flights that lead to delays in delivery and higher shipment cost likewise affect SMEs' competitiveness.

Some of the above constraints can be addressed by economies unilaterally. For example, improvement of investment and business environment, regulatory reforms to improve payment services are policy options that economies can implement on its own. Others may need regional cooperation such as consistency in data privacy rules and

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<sup>13</sup> The amount a credit card merchant pays to the buyer after she successfully disputes a transaction on her statement.

<sup>14</sup> The percentage of website visitors who actually buy.

standards, data flows, competition and customs issues.

*4. Improve customs rules/regulations and clearance process (aka trade facilitation)*

Access to products that are not available locally is one advantage of cross-border e-commerce. Still, to bring foreign products inside an economy requires product certification and registration which can be burdensome for SMEs to comply with. Compounding the difficulty is the inconsistency of applications of rules and regulations across economies, and even in the same economy across different government agents. The ballooning compliance cost often lead to SMEs' expected margin disappearing.

Establishing local presence by locating warehouses or domestic fulfillment centers help cut cost and take advantage of scale economies from the regulatory procedures. Another solution that platform operators resort to is limit sale to products that do not require complicated registration and certification procedures. This, however, tends to exclude many products that SMEs typically produce such as food products or local handicrafts.

To expedite release of products from customs, logistics providers or platform operators self-regulate by, for example, limiting the number of products per package or employing sophisticated x-ray machines or canine teams to screen packages before shipping. Naturally, this increase in cost is passed on to sellers and buyers.

In an effort to address customs challenges from e-commerce, some economies are trying out innovative ways, such as having a special lane specifically for e-commerce. But there are limitations as these are policy experiments. For example, the lane may allow only certain products, or the list contains description of products that is not based on the internationally accepted harmonized system of classification, thus causing confusions and issues of interpretation.

*5. Examine laws on e-commerce-related taxes and duties*

*De-minimis value for import duty*

De-minimis indicates the minimum value of products that are dutiable. Low de-minimis values essentially foreclose growth of cross-border e-commerce as it would subject almost all packages to import duties.

*Product returns and double taxation*

Facilitating returns is integral to e-commerce business strategy to attract consumers but comes at a cost. Besides paying for the reverse logistics, refund processing, and

shipping of replacement product, sellers also pay a new set of taxes and duties (if the product is dutiable) without being refunded for the original duty paid for the returned product. At the moment, there is no clear process in many economies on how sellers can claim back paid taxes and duties for returned products. Additionally, returned packages are, in many economies, treated as new exports or imports and therefore subject to a new set of taxes and duties.

#### *New e-commerce tax*

E-commerce has changed the way people shop and impacted government revenue as well as domestic competition. In response, some economies are implementing forms of e-commerce tax, particularly for digital products and services. Discussions revolving around these type of policies, their effective deployment and impacts are important going forward.

### **Conclusion**

E-commerce provides an alternative route to SME internationalization and hence can contribute to the global agenda on greater inclusion. However, it does not come easily and there are challenges to overcome for e-commerce to be an effective channel. The fact that many SMEs lack awareness of business possibilities through e-commerce and even lack basic business skills means that there is a need to raise more awareness and build capacity among SMEs.

Furthermore, e-commerce has an ecosystem with multiple stakeholders that help make the system work smoothly and efficiently. Good digital infrastructures including ICT, payment services and postal services are some critical components of the ecosystem. Regulations that adversely affect any players in the ecosystem impact the whole, including the buyers and sellers, some of whom are SMEs. In this regard, it is important that economies continue with efforts to improve business environment, develop robust e-commerce ecosystem, and improve customs rules/regulations and clearance process.

The e-commerce landscape is dynamic and continues to evolve. Regular dialogues between relevant stakeholders and policymakers are useful to understand these trends and hear policy developments that may be useful to replicate.



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