

# **Developing Strengths of Small and Medium Enterprises in Taiwan**

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## CONTENTS

I. Introduction.....	1
II. Government Perspective.....	2
A. Encourage Investments and Provide Funding to Stressed SMEs .....	2
B. Facilitate Financing Sources of SMEs .....	2
1. Debt Financing .....	2
2. Equity Financing.....	3
C. Improve Legal Infrastructure For SME Development .....	3
III. SMEs' Perspective .....	4
A. Help Yourself; Do Not Solely Rely on Others.....	4
B. Use All Available Information and Sources.....	4
C. Improve Efficiency of Business Operations.....	5
D. Strengthen Innovation and R&D.....	5
IV. Other Actions .....	6
V. Conclusion.....	6

## APPENDIXES

Table 1: Important Economic Indicators of Taiwan (1995~2001).....	7
Table 2: SMB Guarantee Fund's Performance by Guarantee Item in 1999.....	9
Table 3: SMB Guarantee Fund's Performance by Industry in 1999.....	10
Table 4: SMB Guarantee Fund's Statistics of Guarantee Performance (1974~1999).....	11
Table 5: Listing Rules on Taiwan Stock Exchange, OTC Exchange and TAISDAQ.....	12

# Developing Strengths of Small and Medium Enterprises in Taiwan

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## I. Introduction

Taiwan's solid and flexible economic systems supported by local small and medium enterprises ("SMEs") is regarded as one of the greatest contributors to Taiwan's Miracle. But many of Taiwan's SMEs, with weak management and limited financing sources, are struggling painfully in the slowdown of the economy in Year 2001.

The global downturn which began in the fourth quarter of the year 2000, especially resulting from the Internet bubble having burst in NASDAQ and the poor performance of many high-tech companies, has sharply hurt the Taiwan's economy. Taiwan's unemployment rate hit a historic high of 3.89% in March of this year and is expected to rise rapidly in the next few months. Although the DDP government vowed to defend the targeted 5% GDP growth rate, local private economic research institutions have adjusted their estimate of GDP growth this year down to 4.35%~ 4.75%. The productivity of the manufacturing sector decreased 4.95% in the first quarter this year, for the first time in 26 years. According to the Ministry of Economic Affairs ("MOEA"), 1,330 companies closed in March 2001, up 337% from March of last year, and 2,133 factories closed in the first quarter this year, up 74.9% compared with the same period of Year 2000 (For Taiwan's economic performance from 1995 to 2001, see Table 1).

Bad news has devastated the confidence of consumers and investors in Taiwan. Facing economic recession and transmission of Taiwan's industrial structure, many people are asking "How can Taiwan's SMEs, well known for their flexibility and energy, weather this thunder storm?" This article will provide advice divided into two sections: first the government perspective, and then the SME perspective.

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## **II. Government Perspective**

### **A. Encourage Investments and Provide Funding to Stressed SMEs**

In an effort to reduce unemployment, the first priority of the government is to encourage investments by SMEs, conglomerates and foreigners in Taiwan. The DPP government has proposed a "8100 Plan," to invest NT\$810 billion for a comprehensive public works package. However, we believe that the package of proposals should also include deregulation of labor laws and investment restrictions, improvement of bureaucratic efficiency, encouragement of mergers and acquisitions among SMEs and development of greater political and commercial links between Taiwan and Mainland China. Although the Labor Commission has provided plenty of employment opportunities in its "Constant Employment Engineering Plan" to assist the jobless, the government should take more positive steps to fulfill the gap between the supply side and the need side in the local labor market. The government must provide more job training programs in local areas, relax the qualifications of coverage of unemployment insurance and subsidize those employers hiring middle-aged employees.

In addition, the government might consider offering credit to SMEs, at a favorable interest rate through Small and Medium Business Guarantee Fund ("SMB Guarantee Fund") or local banks, in order to assist SMEs to survive the recession.

### **B. Facilitate Financing Sources of SMEs**

#### **1. Debt Financing**

As with SMEs in other countries, most of Taiwan's SMEs are funded by family members and friends at the start-up stage. However, they will soon run into funding problems if their businesses grow well. It is not easy for new SMEs to obtain financing from banks if the SME can offer no real estate as collateral for its loans from the banks. The SMB Guarantee Fund was established by the government and financial institutions in July 1974 to provide credit guarantees to SMEs which lack real estate or other collateral. From 1974 to 1999, the SMB Guarantee Fund has offered credit guarantees for 1.7 million cases with a total

credit guarantee amount of NT\$2,722 billion, which has benefited 114,046 SMEs. The SMB Guarantee Fund has become one of the major essential funding channels to SMEs in Taiwan. (For the performance of SMB Guarantee Fund, see Table 2 ~ Table 4)

In addition to the SMB Guarantee Fund, the government contributed NT\$9 billion to set up a Small and Medium Business Development Fund ("SME Development Fund"). The SME Development Fund was created to help develop four major objectives: SME project financing, SME support plans, SME development companies, and SME innovation and incubation centers. As of June 2000, 48 SME innovation and incubation centers were established around this country, to provide SMEs with facilities, technological support, management support and information support.

## **2. Equity Financing**

Another new development is that Taiwan's government created the Taiwan Innovative Growing Entrepreneur ("TIGER" or "TAISDAQ") market in 1998. Patterned after NASDAQ, MOTHER in Japan, and GEM in Hong Kong, the TAISDAQ market provides a package of more lenient listing rules for start-up high tech companies. The new TAISDAQ market requires no profitability in order to list a new start-up. This is quite different from the profitability requirement to be listed on the Taiwan Stock Exchange or Over-The-Counter Exchange. Currently, fourteen companies have listed in TAISDAQ. However, since TAISDAQ has adopted rigid trading rules, the trading volume on the TAISDAQ market is considerably below the original expectations. The rigid requirements include a longer lock-up period during which insiders' shares must be deposited in the Taiwan Stock Central Depository Co., Ltd., restrictions on margin trading and short sales, prohibition against investments by local mutual funds and prior settlement reserves for investors. We expect the Securities and Futures Commission will further relax the trading rules of the TAISDAQ market to facilitate greater equity funding to local SMEs. (For a comparison of the listing rules on Taiwan Stock Exchange, the Over-The-Counter Exchange and the TAISDAQ, see Table 5)

### **C. Improve Legal Infrastructure For SME Development**

To maintain the growth of SMEs in Taiwan, the Taiwan Legislative Yuan passed

certain amendments to the Statute of Developments of Small and Medium Enterprises ("Amended Statute") in December 27, 2000.

The Amended Statute requires the MOEA to disclose all sources used by the government for SMEs' development in the Small and Medium Enterprises White Book annually. This requirement will help the MOEA to periodically review its policies of assisting in the development of SMEs. The Amended Statute also requires the government to consider the size and features of SMEs when drafting or amending any SME-related laws and regulations and to report to the Legislative Yuan three months before the end of each year concerning the effects of such laws and regulations. To guarantee a stable financing source for SMEs, the Amended Statute also requires banks to increase their contributions to thirty-five percent (35%) of the total capital of the SMB Guarantee Fund. The above changes will further develop the strengths of SMEs in Taiwan.

### **III. SMEs' Perspective**

#### **A. Help Yourself; Do Not Solely Rely on Others**

SMEs should not solely rely on others, including reliance on government support, in developing their businesses. Although outside support is essential to SMEs, most of the problems can only be solved by each SMEs individually rather than by others. SMEs must recognize that a government with limited manpower and finances only serves as a supporter to SMEs rather than as mighty God. Corporate officers and personnel cannot sit in the office and daydream that the government will show up to resolve all of their problems. While government assistance is important, it is essential that SMEs employ the hardwork and creative solutions that are key to success.

#### **B. Use All Available Information and Sources**

Constrained by limited manpower, funding and management, SMEs often encounter difficulties obtaining information regarding outside support, even if the government or private sectors (including financial institutions) are willing to provide assistance to them. Thanks to technology innovations, such as the Internet and e-mail, people in remote areas can communicate more efficiently and conveniently. SMEs should have easy access to the homepage of the Small

and Medium Enterprises Administration, MOEA (<http://www.moeasmea.gov.tw>), which provides plenty of information regarding telephone numbers of relevant agencies, subsidies, management advice, funding, technology supports, legal services and seminars. In order to solve various problems faced by SMEs, the Small and Medium Enterprises Administration has also set up a "quick processing center," as a one-step window to coordinate the relevant government agencies and available source providers. The government also provides various funding supports and subsidies through the banking system, local governments and the SMB Guarantee Fund. SMEs may obtain relevant information for free or at very low cost through these channels, and then have the ability to decide how to utilize these sources to manage their businesses more efficiently and profitably.

### C. Improve Efficiency of Business Operations

In a sluggish economy, it is difficult for SMEs to develop new business or explore new customers. In order to earn profits, SMEs may wish to review the procedures of their daily operations and work on cutting nonessential costs and expenses. For example, several years ago, a local bank adopted a proposal provided by its employees to combine the monthly bill to its credit card holders with the GUI (an invoice to customers required by the tax authority) and it saved ten of millions of NT dollars in annual mailing charges. It is often easier for SMEs to improve the efficiency of business operations internally than to find new sources of revenue in a down market.

### D. Strengthen Innovation and R&D

Profitability comes from innovation, research and development. In the period of the 1960s to 1980s, Taiwan's SMEs relied heavily on labor-intensive businesses because of their lack of funding, management and technology. However, various developing countries in the Asian region, such as Mainland China, Thailand, Malaysia and Vietnam, have been offering abundant laborers, lands and infrastructure to foreign investors at low costs, which has cut into the competitiveness of Taiwan's SMEs.

Accordingly, in the recent years, Taiwan's SMEs have turned to knowledge-based industries, including personal computers, scanner, monitors and printed circuit boards, or value-added products, such as frozen processed sea

eels, bicycles and sewing machines. This progression helped Taiwan to earn its name as the "Technology Island" in recent years. Taiwan's SMEs also invest globally to diversify their productivity bases and increase their marketing channels in various foreign markets. These achievements are derived from the SMEs' long-term efforts in technology innovation and R&D. When the economy slows down, the SMEs who are positioned to provide value-added products or knowledge-based services to their customers are more likely to survive the storm than their competitors.

## **IV. Other Actions**

In addition to creating a friendly environment for SMEs' further developments, we believe that the following actions should also be taken by the government, private sector and SMEs together in order to ensure the global competitiveness of Taiwan's SMEs:

- Foster an environment conducive to creative and independent education;
- Promote knowledge-based entrepreneurship;
- Encourage technology innovation, E-commerce developments and Internet access by SMEs;
- Facilitate financing sources of SMEs, including venture capital, capital market, banks and government-supported funds; and
- Develop a sound corporate governance system that supports further developments and management of SMEs.

## **V. Conclusion**

Taiwan's SMEs are facing a turning point at this difficult moment of Taiwan's depressed economy. The transmission of industrial structure in Taiwan from a labor-intensive economy to a knowledge-based economy and the global recession, especially in the high tech industry, have created a dilemma for future developments of Taiwan's SMEs. In order to sail through the thunderstorm, we believe, the government must encourage investments, facilitate funding sources of SMEs and improve the legal framework for SMEs' developments. As for the SMEs, we advise that SMEs should help themselves than solely relying on outside support, use all available information and sources,

improve efficiency of business operations and strengthen their abilities through innovation and R&D.

**Table 1: Important Economic Indicators of Taiwan**

Update: April 27, 2001

Items		Unit	1995	1996	1997	1998	1999	2000	2001
<b>I Economic Indicators</b>									
Economic Growth	1.Economic growth rate	%	6.42	6.10	6.68	4.57	5.42	5.98	(f)
	2.GNP	100 Million US\$	2,691	2,836	2,933	2,692	2,905	3,144	(f)
	3.Per capita GNP	US\$	12,686	13,260	13,592	12,361	12,325	14,216	(f)
	4.Gross national savings/GNP	%	27.0	26.7	26.4	26.0	26.1	25.2	(f)
Production (annual changes)	1.Industrial production	%	4.7	2.0	7.4	2.6	7.5	7.4	Mar.
	2.Manufacturing production	%	5.2	2.9	8.7	2.4	7.9	8.0	Mar.
	Heavy industry	%	9.6	4.8	13.1	4.6	10.7	11.1	Mar.
	Light industry	%	-2.7	-0.8	-0.7	-3.1	0.5	-1.0	Mar.
	3.Floor areas applying for construction permits	%	-25.4	-17.5	21.5	-5.9	-13.2	-5.8	Feb.
	4.Floor areas granted occupancy permits	%	-5.0	-17.3	-15.9	0.6	6.6	-15.1	Feb.
	5.Applications for closing factories?	Establishments	5992	5,339	2,904	6,788	3,982	4,995	Jan.
	6.Factory newly opening registration	Establishments	6905	5,414	6,039	5,726	5,846	5,689	Jan.
	7.Structure of domestic production: Agriculture	%	3.5	3.2	2.6	2.5	2.6	2.0	
	Industries	%	36.4	35.7	35.3	34.5	33.2	32.4	
	Services	%	60.1	61.1	62.1	63.0	64.2	65.6	
	8.Small and medium size enterprises								
	Establishments(% of registered profit-oriented business enterprises)	%	98.0	98.0	97.8	97.8	97.7	...	
	Employed persons(% of total employed persons)	%	79.8	78.6	78.4	78.2	78.3	...	
	Employees on payrolls(% of total employees)	%	70.8	69.2	69.3	69.2	69.3	...	
Revenue(% of registered profit-oriented business enterprises)	%	36.0	34.3	32.1	30.4	28.4	...		
Exports (% of total exports)	%	50.7	49.8	48.8	46.6	21.1	...		
Investment	1.Growth rate of fixed capital formation	%	7.3	1.7	10.7	8.0	1.8	7.8	(f)
	2.Growth rate of private fixed capital formation	%	11.4	3.4	18.6	11.8	-0.7	13.7	(f)
	3.Annual changes of approved foreign investments	%	79.4	-15.9	72.7	-12.4	13.2	79.8	Feb.
	4.Increase rate of capital goods imports	%	24.0	8.8	18.5	11.9	20.3	34.3	Feb.
Trade (annual changes)	1.Imports on customs basis	%	21.3	-1.1	11.8	-8.5	5.8	26.5	Mar.
	2.Exports on customs basis	%	20.0	3.8	5.3	-9.4	10.0	22.0	Mar.
	3.Balance of foreign trade	100 Million US\$	81.1	135.7	76.6	59.2	104.9	83.6	Mar.
	4.Export orders received	%	20.1	4.8	4.1	-4.0	7.3	20.4	Mar.
	5.Foreign exchange	NT\$/US\$	27.30	27.5	32.6	32.2	31.4	31.4	Apr. 27
Banking	1.Foreign reserves	100 Million US\$	903.1	880.4	835.0	903.4	1062	1,067	Feb.
	2.Rediscout rate	%	5.5	5.0	5.3	4.8	4.5	Dec. 29	4.7
	3.Past-due loan ratio of financial institutions (end of period)	%	3.00	4.15	4.18	4.93	5.67	Dec.	6.20
	4.Dishonored check ratio in amount	%	0.52	0.44	0.32	0.36	0.49		0.48
	5.Government foreign debt (June 30)	100 Million NT\$	55.8	39.2	24.8	18.8	10.6		8.0
	6.Stock price index (average)	1966=100	5,544	6,004	8,411	7,714	7,427		7,847
	(end of period)	1966=100	5174	6,934	8,187	6,418	8,449		4,739
	7.Stock trading value per day	100 Million NT\$	355	448	1302	1093	1101		1,126
8.Annual changes of M2	%	11.6	9.2	8.3	8.8	8.3		7.0	
Labor Force	1.Labor force participation rate	%	58.7	58.4	58.3	58.0	57.9	57.7	Mar.
					M: 71.1	M: 70.6	M: 69.9	M: 69.4	Mar.
					F: 45.6	F: 45.6	F: 46.0	F: 46.0	Mar.
	2.No. of employed persons	10thousand	905	907	918	929	939	949	Mar.
	3.Percentage distribution of persons employed: Agriculture	%	10.5	10.1	9.6	8.9	8.3	7.8	Mar.
	Industries	%	38.7	37.5	38.2	37.9	37.2	37.2	Mar.
Services	%	50.8	52.4	52.2	53.2	54.5	55.0	Mar.	
4.No. of unemployed persons	10thousand	16.5	24.2	25.6	25.7	28.3	29.3	Mar.	
5.Unemployment rate	%	1.79	2.60	2.72	2.69	2.92	2.99	Mar.	
6.Annual changes of labor productivity of manufacturing establishments	%	7.4	5.4	7.0	4.4	7.05		6.12	

Explanation: (f) forecasted.

**Table 2: SMBGuarantee Fund's Performance by Guarantee Item in 1999**

Unit: NT\$1,000

Item of Credit Guarantee	Number of Guarantees	Guarantee Amount	Outstanding Credit Covered by Guarantees	Percentage
General Purpose Loan	57,765	91,918,660	92,599,582	67.0
Small-amount Working Capital Handy Loan	1,839	2,022,932	1,900,475	1.4
Bank Guarantee on SMEs' Commercial Paper	333	931,658	691,065	0.5
Export Loan	2,825	3,269,946	1,571,133	1.1
Loan for Raw Materials	29,106	30,445,928	24,044,722	17.4
Guarantee on Import Duty & Tax on Accounts	13	2,022	1,804	0.0
Small-scale Business Loan	582	319,625	454,076	0.3
Guarantee on Contract Performance	1,438	2,701,880	3,555,569	2.6
Policy-oriented Loan	913	3,443,674	11,568,005	8.4
Youth Business Start-up Loan	490	223,835	758,409	0.5
Own Brand International Promotion Loan	6	22,224	264,923	0.2
Development Loan	41	182,480	900,155	0.7
<b>Total</b>	<b>95,351</b>	<b>135,484,865</b>	<b>138,269,918</b>	<b>100</b>

Source: Annual Report of SMB Guarantee Fundin 1999, Page 20

**Table3: SMB Guarantee Fund's Performance by Industry in 1999**

Unit: NT\$1,000

Industry	Number of Guarantees	Guarantee Amount	Outstanding Credit Covered by Guarantees	Percentage
Machinery & Metal Products	11,708	19,164,738	21,400,795	15.5
Textile & Clothing	2,851	4,767,156	5,745,282	4.2
Electric Machinery & Electronics	8,251	13,582,014	12,471,107	9.0
Food	1,069	1,965,624	2,373,765	1.7
Plastics	3,771	5,487,942	5,993,091	4.3
Rubber	476	644,943	645,707	0.5
Wood & Non-metallic Products	824	1,114,084	1,305,989	0.9
Transport Equipment	1,156	2,235,513	2,936,921	2.1
Shoe Manufacturing	128	239,589	274,646	0.2
Non-Metallic Mineral Products	1,241	2,312,930	2,617,958	1.9
Chemicals	1,145	1,729,307	1,834,622	1.3
Stationary Toys & Sport Products	703	1,077,612	1,285,408	0.9
Printing & Paper Products	1,444	2,356,350	3,617,407	2.6
Jewelry & Crafts	78	157,800	192,893	0.1
Other Manufacturing	1,017	1,641,286	1,854,616	1.3
Construction	2,913	7,780,541	7,100,016	5.1
Manufacturing Business (sub-total)	38,775	66,527,428	71,650,224	51.8
Agriculture, Forestry, Fishing & Livestock	295	829,395	855,918	0.6
Mining & Quarrying	135	303,116	415,885	0.3
Gas Supply	7	13,560	17,613	0.0
Maintenance & Repair Services	3,231	5,216,224	5,367,566	3.9
Export & Import	4,341	4,667,339	4,769,490	3.4

Trade				
Other Trade	43,286	51,475,025	47,523,981	34.4
Transport & Storage	1,370	2,133,033	2,333,343	1.7
Business Service	1,722	2,481,773	2,570,221	1.9
Social & Individual Services	827	1,337,572	1,332,504	1.0
Non-manufacturing Business (Sub-total)	55,214	68,457,036	65,186,521	47.1
Small-scale businesses	872	546,565	674,764	0.5
Youth Business Start-up	490	223,835	758,409	0.5
<b>Total</b>	<b>95,351</b>	<b>135,484,865</b>	<b>138,269,918</b>	<b>100.0</b>

Source: Annual Report of SMB Guarantee Fundin 1999, Page 21

**Table 4: SMBGuarantee Fund's Statistics of Guarantee Performance  
(1974~1999)**

Unit: NT\$ Million

Year	Net Worth	Cases Guaranteed	Amount Guaranteed	Total Amount Supported	Outstanding Credit Covered by Guarantee	Outstanding Credit Supported	* Outstanding Credit Covered by Guarantee /Outstanding Credit to SMEs (%)
1974-1985	(1985) 3,329	406,598	276,568	341,776	(1985) 41,550	(1985) 52,446	
1986	3,545	88,733	74,295	92,537	47,007	59,992	10.4
1987	4,260	92,159	81,010	102,705	53,312	68,913	9.3
1988	5,930	81,783	77,942	99,198	57,002	73,768	6.9
1989	8,470	73,405	77,606	98,743	59,147	76,509	5.7
1990	9,869	65,551	76,867	97,723	61,514	79,251	5.2
1991	11,808	79,704	112,623	143,521	86,294	110,999	5.8
1992	12,743	90,603	135,985	173,941	105,351	135,863	5.7
1993	13,852	103,218	161,744	208,533	125,700	163,031	6.1
1994	15,376	114,294	183,974	238,690	146,117	190,515	6.3
1995	15,622	117,250	193,079	255,350	157,309	209,254	6.6
1996	15,327	100,952	160,911	225,259	150,862	209,505	6.6
1997	15,461	99,198	154,785	224,762	145,650	208,982	6.1
1998	13,436	92,842	141,045	210,204	142,851	209,769	6.1
1999	13,437	95,351	135,485	208,609	138,270	208,940	6.1
<b>Total</b>	-	<b>1,701,641</b>	<b>2,043,920</b>	<b>2,721,551</b>	-	-	-

Source: Annual Report of SMB Guarantee Fundin 1999, Page 22

**Table5: Listing Rules on Taiwan Stock Exchange, OTC Exchange and TAISDAQ**

	<b>TSE</b>	<b>OTC</b>	<b>TAISDAQ</b>
<b>Incorporation Period</b>	5 years	3 years	1 year
<b>Minimum Paid-in Capital</b>	NT\$600 million	NT\$100 million	NT\$30 million
<b>Accumulative Losses</b>	No accumulative losses in the last fiscal year	No accumulative losses in the last fiscal year	May be Waived
<b>Profitability Requirements</b>	1. 6% in the last two fiscal years 2. an average of 3% in the last five fiscal years	1. 2% in the last two fiscal years 2. 4% in the last fiscal year	X
<b>Lock-up Period for Insiders</b>	2 years	2 years	4 years
<b>Margin Trading and Short Sale</b>	O	O	X
<b>Purchased by Local Mutual Funds</b>	O	O	X
<b>Purchased by Dealers and QFIIs</b>	O	O	O