CHAPTER II

REVIEW OF LITERATURE
2.1. INTRODUCTION:

This review of literature is intended to present the work already done in the field of challenges of MSMEs and Cluster Development so as to understand the concepts and issues. Therefore, this chapter is divided into two sections in which

- Section I deals with studies on Challenges of MSMEs
- Section II reviews studies on Cluster Development

2.2. CHALLENGES OF MSMEs:

The major advantage of the MSME sector is its generating employment at low cost. The MSME sector is highly heterogeneous. There are different size of the enterprises, variety of products and services and level of technology. It helps in the industrialization of rural and backward areas. It reduces regional imbalances. It provides equitable distribution of national income and wealth².

MSMEs are the backbone of the Indian economy. They contribute in GDP and GNP of India. It acts as a breeding ground for entrepreneurs to grow from small to big. MSME Sector are increasing enormously in India³.

² http://www.dnb.co.in/SME_cluster_series2012_Nagpur/PDF/MSMEs_in_India.pdf
³ India’s new economic policy- Rudra Dutta
India has nearly 12 million MSMEs, which is almost 50% of industrial output and 42% of India’s total export. The reasons are investment of less capital, high contribution to domestic products, extensive promotion and support by Government, significant export earnings, operational flexibility, manpower training, machinery procurement, capacity to develop appropriate indigenous technology and technology-oriented industries\(^4\).

According to the latest reports by the SMB Chamber of Commerce\(^5\) and the Ministry of Micro, Small and Medium Enterprises, India currently has more than 48 million SMEs. Small and Medium Enterprises (SMEs) in India have seen exponential growth over the last decade.

SMEs contribute more than 45% of India’s industrial output, 40% of the country’s total exports and create 1.3 million jobs every year and it continues to struggle on multiple accounts. While some are challenged by credit and finance issues, others are struggling to cope with stringent regulatory environments\(^6\).

\(^4\) Annual Report 2010-11 Govt. of India, Ministry of Micro, Small and Medium Enterprises

\(^5\) “According to the latest reports by SMB Chamber of Commerce and Ministry of Micro, Small and Medium Enterprises, India currently has more than 48 million SMEs” Source: Malini Goyal, “SMEs employ close to 40% of India’s workforce, but contribute only 17% to GDP”, Economic Times, June 9, 2013

According to the latest Annual Report issued by the Ministry of Micro, Small and Medium Enterprises\(^7\), there are over 6,000 products, ranging from traditional to high-tech, which are being manufactured by the MSME sector for domestic as well as international markets.

After the agriculture sector, SMEs rank second in fostering employment opportunities. Over 3.25 lakh jobs were generated in the SME sector during the period between April 2011 and February 2012\(^8\).

Funds focussing on SMEs are having difficulties in raising money because of the prevailing conditions. The total gap in MSME funding is estimated at USD 126 million. Although banks have been slowly trying to bridge this gap, stringent reforms from the government are required\(^9\).

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\(^7\) “According to the Annual Report issued by the Ministry of Micro, Small and Medium Enterprises, there are over 6000 products, ranging from traditional to high-tech which are being manufactured by the MSME sector for domestic as well as international markets.” Source: Ministry of MSME Annual Report 2012 – 13, (http://msme.gov.in/WriteReadData/DocumentFile/ANNUALREPORT-MSME-2012-13P.pdf)

\(^8\) “Over 3.25 lakh jobs were generated in the SME sector during the period between April 2011 and February 2012” Source: Express News Service, “State ranked 3rd for generating 30,000 jobs in SMEs”, Indian Express, July 25, 2012, (http://indianexpress.com/article/cities/lucknow/state-ranked-3rd-for-generating-30-000-jobs-in-smes/)

\(^9\) “Funds focussing on SMEs are having difficulties in raising money because of the prevailing conditions. The total gap in MSME funding is estimated at USD 126 million” Source: Rajiv Janjanam, “What financiers do when funding an SME, and what they can do better”, Economic Times, June 12, 2014 (http://articles.economictimes.indiatimes.com/2014-06-12/news/50536526_1_indian-smes-msmes-funding-gap)
According to World Bank, India has slipped 3 ranks in its Ease of Doing Business Index – this raises deep concerns about the state of affairs in India. SMEs are said to be the backbone of India’s economy, however not much is being done to promote their healthy growth and development\textsuperscript{10}.

India scores very low on the World Bank’s Ease of Doing business Index and this is primarily because India does not provide a very favourable business climate for its enterprises, especially the SMEs. Indian SMEs are weighed down by inflexible and complicated regulatory policies which make starting and running a business difficult. Owing to this prohibitive business climate, many innovative entrepreneurs are not able to enter the markets or sustain a business\textsuperscript{11}.

There are multiple government schemes and programs under which SMEs can access technology. However, education and awareness about these initiatives is dismally low. 90% enterprises remain unaware about Technology Business Incubation (TBI), one of the government’s key initiatives\textsuperscript{12}.

\textsuperscript{10} \url{http://www.thehindu.com/business/Industry/india-slips-three-spots-in-ease-of-doing-business/article6026229.ece}

\textsuperscript{11} “Indian SMEs today operate in a very challenging atmosphere. According to World Bank, India has slipped 3 ranks in its Ease Doing Business Index” Source: Special Correspondent, “India slips three spots in ease of doing business”, The Hindu, May 19 2014,

\textsuperscript{12} Technology Business Incubation (TBI) is one of the most recent services that NSIC has initiated. TBI enables technical entrepreneurs to conduct their R&\textsuperscript{D} programmes in a professional, friendly and supportive environment, while receiving the guidance and hand holding they need in the initial phase. This facility is being offered in Information Technology, Product Design, Energy and Environment auditing, Bio-Technology Electronics and Communications. Source: “FICCI GT Report on Vison2020 – Implications for MSMEs”, February 18, 2011, \url{http://www.ficci.com/spdocument/20143/Grant-Thornton-FICCI%20MSME.pdf}
As an ongoing effort, the government runs multiple schemes and programs to support SMEs with access to knowledge, technology and funding to tackle marketing and supply chain challenges. However, education and awareness about these initiatives remains very low. 89% enterprises remain unaware about key government initiatives like The Marketing Assistance and Technology Up-gradation Scheme for Micro Small and Medium Enterprises and the MSE Marketing Development Assistance (MDA) Scheme.

Indian SMEs employ 40% of the country’s workforce, making them the employment powerhouse of the country. However, India today faces the big challenge of outdated labour laws that are still in use. This leaves many SMEs struggling with problems of culture and scale and not being able to meet their workforce demands. A labour law reform overhaul is required to absorb the 200 million individuals that will enter the workforce in the next 2 decades.

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14 “A labour law reform overhaul is required to absorb the 200 million individuals that will enter the workforce in the coming 2 decades” Source: Rajesh Kumar Singh, “India’s Modi eyes first labour overhaul in decades to create jobs”, UK Reuters, June 29, 2014 (http://uk.reuters.com/article/2014/06/29/uk-india-labour-reforms-idUKKBN0F40XZ20140629)
A recent study by ASSOCHAM confirmed that this new wave of leadership for India is expected to double foreign investments to USD 60 billion. This is surely a major boost from the distressed condition of the Indian economy under the previous UPA government. While it’s hard to miss the air of optimism in the country, longevity of this sentiment is contingent on the announcements in the Union Budget. SMEs continue to be plagued with challenges that are inhibiting them from growth in revenue and scale. The Union Budget 2013-14 did little to uplift the sentiments of the SME sector and offered no additional support and guidance. SMEs expect the new Narendra Modi-led NDA government to focus on their key challenges and provide definitive schemes and programs to help solve long pending matters.

According to Jajri et. al. (2009), even though with large number of establishments, SMEs contribution to output, value added and fixed asset is far below of that by the large scale industries. Though small and medium scale industries are considered backbone in economic growth in all country, not many companies seriously tries to make quality control program work. As demand increases manufacturer generally go for higher & higher production neglecting quality ultimately loosing customers.

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15 “The newly appointed government in India has worked like a shot in the arm for the country’s economy. A recent study by ASSOCHAM confirmed that this new wave of leadership for India is expected to double foreign investments to USD 60 billion.” Source: “Banking on Narendra Modi, foreign investors to pour $60 billion into India: Study”, Economic Times, May 25, 2014, (http://articles.economictimes.indiatimes.com/2014-05-25/news/50083679_1_fdi-inflows-fii-investment-indian-economy)

Singh, Garg and Deshmukh (2006)\textsuperscript{17} observed that the SMEs are reluctant for changes due to fear of failure. In general, SMEs are slow to adopt technology & pay lower wages than larger firms. Therefore, smaller firms may be last in the queue for highly skilled labour.

Most OECD governments promote entrepreneurship and seek to support and develop SMEs through a myriad of policies and programs. The attempts to combat many of the common difficulties encountered by SMEs and offer solutions to problems in such areas like finance, technology, innovation, IT, management, internationalization etc (Rodriguez et.al. 2007)\textsuperscript{18}.

According to RajivKumar, et.al. (2002)\textsuperscript{19}, the flat organizations allow for more efficient information flows, faster communication, greater flexibility, greater adaptability, and reduced costs, and encourage innovative ideas to flourish. In order to be flexible and adaptable, organizations need to be less formal and less centralized.

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\textsuperscript{18} Rodriguez Dr.Placid, Dasgupta Sh. Anupam, Patwardhan Prof. Anand, Mittal Dr. H. K., Nagpal Dr. Sarita., Karunakaran Dr. T, Saxena Dr. Neeraj, “Science & technology for small & medium scale enterprises (SMEs)”, Report for the eleven five year plan (2007-2012).

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With the WTO regime of removing trade barriers and increased globalizations, today, SMEs will need to compete with their counterparts from other parts of the world. While Indian players have the cost advantages due to availability of cheap labor and government incentives for the sector, they will need to build their strengths on the technology front and management and marketing skills in order to survive in the global market. While we look into new approaches to strengthen SMEs and sustain economic growth, one has to understand the limitations, stated by Rahman, Zain, Nopiah, Ghani, Deros, Mohammad & Ismail (2009)20

The long-term involvement of large buyers with extensive global connections in SME-dominated clusters from developing countries has often proven to be beneficial. These buyers can improve the ability of SMEs to compete in the global marketplace by “communicating clear-market requirements, providing support on logistical issues and participating in quality improvement programmes” (ITC, 2005)21.

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Thiripurasundari, K and V. Gurumurthy (2009)\textsuperscript{22} highlighted the challenges of micro, small and medium enterprises of India. One side the globalization is an opportunity as well as another side it is a challenge for the indigenous MSME’S. The Indian MSME’S are facing a great problem due to larger production of foreign manufacturing concern. The financially strong MSME’S will survive strongly at globalized platform.

Nalabala Kalyan,Kumar. Sardar, Gugloth. (2011)\textsuperscript{23} focuses upon the growth pattern of the MSME’S, employment generation (1992-2009). Further, study reveals the symptoms and steps involved in industrial sickness. The study gives the ample amount of knowledge about the various credit schemes sponsored by the government. Laghu udyami credit card scheme, Credit guarantee fund trust for small industries, Swarojgar credit card scheme, Credit linked capital subsidy scheme and credit through commercial banks are the sources and schemes available to fulfil the financial needs as well as financially strengthen to the MSME’S.


Sudan, F. K. (2005)\textsuperscript{24} described the challenges in Micro and Small Scale Enterprises Development and policy issues by arising different questions related to Micro and Small Enterprises. The study explained the meaning, advantages, problems and policy options of MSE sector. The study concluded that all the policies which were opted by GOI were the efforts to form a dynamic MSE sector and a diversified economy providing expanded employment opportunities to absorb all new labour force and offer exciting career opportunities.

Rathod, C. B. (2007)\textsuperscript{25} described the importance of small scale industrial sector and also the contribution of Indian small scale entrepreneurs in world economy. The main objective of the study was to study the growth and pattern of the SSI sector and identify the reasons for success/failures, to evaluate the impact of globalization on SSIs and export opportunity, to identify the barriers and constraints that SSIs were facing to cope with globalization.


UNIDO (1969) in a study based on evidence from a number of developing countries indicated that small enterprises with a lower level of investment per worker tend to achieve a higher productivity of capital than do the larger, more capital intensive enterprises.

Singh et al. (2012) analyzed the performance of Small scale industry in India and focused on policy changes which have opened new opportunities for this sector. Their study concluded that SSI sector has made good progress in terms of number of SSI units, production & employment levels. The study recommended the emergence of technology development and strengthening of financial infrastructure to boost SSI and to achieve growth target.

Bargal et al. (2009) examined the causal relationship among the three variables GDP, SSI output and SSI exports and also have compared the performance parameters of SSIs in the pre and post liberalization era. The study found that the annual average growth rate of different parameters of SSIs have declined in the period of nineties vis-à-vis the pre-reform years. There is an absence of any lead-lag causal relationship between exports and production in small-scale sector and GDP of Indian economy.

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Bodla, B. S. (2004)\(^{29}\) concluded that SSI has produced the maximum attainable output given the inputs of capital and labour and the available existing technology. It has also been observed that the SSI sector is no way less than its counterpart large scale industries in so far as the utilization of resources is concerned.

Hashim (2004)\(^{30}\) has provided an insight into the strengths and weaknesses of small and medium-sized enterprises. It can also be concluded that there are certain weaknesses that prevail in SMEs and need to be removed.

Hussain, V, Syed. (2004)\(^{31}\) analyzed that to survive in the world market SSIs should have to lay greater emphasis on international standards with regard to quality, health and hygiene to be offered by them.


Sahoo, K, Sukanta. (2004) examined the contribution of SSI in the industrial sector and concluded that with the decline in agricultural employment and virtual stagnation in the organized manufacturing sector, employment in SSI sector has emerged as the only ray of hope.

Kansal et al. (2009) In their study, an attempt has been made to analyze the impact of globalization on the growth of small scale industries. The comparative analysis of growth pattern of key parameters between Pre and Post Globalization periods reveals that the “globalization” had a negative impact on the growth of small scale sector measured in terms of number of units, production, employment and exports. It shows that globalization had a negative impact on the growth of SSI.

Garg, Ishu. And Walia, Suraj. (2012) confirms that the significant growth of MSMEs have been taken place over a period of time and this sector is the major donor to gross domestic product (GDP), employment and exports in Indian economy using the OLS technique.

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Absence of adequate and timely supply of bank finance, limited capital and knowledge, lack of power, low quality inputs, low return, non availability of suitable technology, low production capacity, ineffective marketing strategies are the main problems of MSMEs in India. (Shiralashetti, 2012)\textsuperscript{35}.

Accordingly to Spangenberg (2004)\textsuperscript{36}, sustainable development is based on the integration of four dimensions: the economic, the environmental, the social and the institutional and is perhaps the most challenging policy concept ever developed.

He derived four key problem areas related to sustainable development

- The environmental challenge, the degradation of the natural basis of human life;
- The first social challenge, the increasingly unequal distribution of income and assets;
- The second social challenge, the high number of people living in poverty;
- The institutional challenge, the resulting threats to peace and security.


Lack of capital, business information, technology, and skilled workforce, difficulties in procuring raw materials, marketing and distribution challenges, and govt. policy and regulations are the main constraints’ faced by SMEs. Theses constraints may differ from region to region, between sectors, or between individual enterprises within a sector. (Tambunan, 2011)37.

Formal financial intermediaries, such as commercial banks, usually refuse to serve poor households and micro-enterprises because of the high cost of small transactions, lack of traditional collateral, lack of basic requirements for financing and geographic isolation. (Report of Rebobank, Nederland, 2005)38

The typical SME has limited resources, limited cash flows, few customers, is often engaged in management ‘fire-fighting’, concentrates on current performance rather than taking a strategic focus, often has a flat organizational structure and possibly high staff turnover (Hudson et al., 2001)39.


38 Access to financial services in developing countries. Rebobank, Economic Research Department, Nederland (2005).

39 Hudson M, Lean J, Smart P A, 2001, "Improving control through effective performance measurement in SMEs" Production Planning & Control 12 (8) 804-813
The seminal model for credit rationing has been developed by Stiglitz and Weiss (1981)\textsuperscript{40}. The most severe form of a credit rationing is a “credit crunch” that occurs when the supply of credit is restricted below the range usually identified with prevailing market interest rates and the profitability of investment projects.

There is empirical evidence for credit crunch effects during crises, but these effects may vary across firms and, as in the current global financial crisis, also across economies. Especially in the current crisis, strong policy support has attenuated or abated the risk of a true or more severe credit crunch. While it may therefore be hard to draw strong conclusions about the precise occurrence and extent of a credit crunch during this crisis, the measures taken to support lending especially to SMEs were likely the right response to the crisis given that policy makers want to err on the downside rather than on the upside (OECD, 2010)\textsuperscript{41}.


2.3. CLUSTER DEVELOPMENT:

Baptista and Swann (1998)\(^{42}\) suggested that organizations in clusters were more products innovative.

Carrie (1999)\(^{43}\), the original concept of clusters referred to organizations in the same geographical location and industry that used the advantage of “geographical proximity” to gain competitive advantage. He also asserted that global competitiveness implies that future business competition will be between clusters of interrelated organizations that generate value by co-operating. The development of organizational clusters will have a huge impact on business configuration and consequently the supply chains associated with the clusters. The potential implication for the development of operative clusters, firstly as a collective and secondly for individual businesses within the cluster would be significant, particularly in terms of global competitiveness. It is important that the operations management community makes a contribution to the understanding of this development.


Yoguel (1998)\textsuperscript{44}, in recent years, the competitiveness of small and medium enterprises (SMEs) in Brazil has been influenced by increased international competition and environmental restrictions. SMEs have been focused on satisfying local demand within the domestic market. Owners, administrators and managers did not perceive market opportunities and had little control over organizational processes.

Nadvi, 1999\textsuperscript{45}, Rabellotti, 1999\textsuperscript{46}, Karaev et al. 2007\textsuperscript{47}; Solvell et al., 2008\textsuperscript{48}, Carpinetti et al. 2008\textsuperscript{49} The existence of a cluster promotes and facilitates cooperation among companies and can bring about production flexibility, in terms of volume and variety, reduction of production and transaction costs, and development of technological innovations, especially where there is a “local innovation system” supported by nearby universities and research centres.


Brown and Lockett (2001)\textsuperscript{50} defined e-clusters as, “digital enterprise communities enabled by one or more intermediaries and based on a new type of electronically enabled inter-organizational system”.

According to Kuei-Hsien et al. (2008)\textsuperscript{51} and Miles et al (1993)\textsuperscript{52}, Innovation and improvement in product and process development are critical factors to enhance cluster efficiency. They stated that relationships within the chain can differentiate its value when the partners are engaged in common interest activities in a specific sector enabling improvements of proactive actions for the final product or service in a stimulating environment.

Solvell et al. (2008)\textsuperscript{53} added that for a region to making a high level of economic prosperity, it has to be able to provide competences that differentiate their companies from others outside the cluster. According to those authors some conditions in a cluster allow companies to have access to qualified human resources, a variety of suppliers and an implicit knowledge of the peculiarities of the production process among others, which if properly used, improve the competitiveness of a company.


Keeble and Wilkinson (1999)\textsuperscript{54} identified three different mechanisms to spread knowledge considering that the intellectual capacity allows the cluster to be considered a set of competences; workforce mobility among companies, interaction between suppliers and clients, equipment manufacturers and capital goods, establishment of new companies through the current ones and the establishment of centers for workforce training and specialized professional development. The determining factors for the spreading of knowledge lie in the cluster surroundings, i.e. external environmental variables which create conditions that are favorable for implementing such as technical, structural and methodological factors.

Rosenfeld, Liston, Kingslow & Fromm, 2000; Austrian, 2000\textsuperscript{55} was argued network governance theory that a qualitative methodology can go more in depth potentially identifying emerging clusters and better capturing the inter-relationships within the cluster and among the multiple actors that support and enhance the cluster.


Concept for the Improvement of Regional Policy in the Russian Federation (2009)\textsuperscript{56} development by Russia’s Ministry for Regional Development defines zones of accelerated economic growth. These zones are planned to become the platform for organizing territorial production clusters and unified technological chains for manufacturing high value-added goods as the main contribution to the economies of their respective constituents of the Russian Federation. This is the most important regional policy strategy.

Marshall, 1920\textsuperscript{57} explained that the industrial cluster plays a critical role in the promotion of industrial development because it facilitates the specialization and division of labor among enterprises, information spillovers and the formation of various labour markets.

Henderson and Kuncoro, 1996\textsuperscript{58} stated that industrial development is often associated with urbanization because urban areas have improved transportation and communication facilities, which in turn attract various industries to these areas.


J.L. Truel\textsuperscript{59} pointed out a dramatic increase in a number of SME within the French clusters, which had been keeping a traditional focus on the large corporations for a long time. Since 2005, small and medium-sized companies became paramount numerically as well as in gaining support. Forms of cooperation include mostly the outsourcing of short-run production, cooperation in research, but there are some examples of independent small-scale enterprises’ incorporation in the large corporations’ organizational structure.

While the growth rate is expected to diminish to 6% - 7% during 2008 – 2009, many analysts predict that India’s growth is likely to continue into the future with an average annual rate of 6.3% from 2008 to 2030. Much of India’s growth has been led by the service and manufacturing sectors, which is expected to grow at 10.7% and 9.4% growth, respectively in 2008 – 2009 according to India’s Finance Minister, P. Chidambaram\textsuperscript{60}, as stated in his 2008 – 2009 union budget address.

\textsuperscript{59} J.L.Truel, \textit{Implementing a successful cluster policy: some clues from the French experience}, University Paris 12, 2011

Accordingly to a Nasscom – McKinsey Report\textsuperscript{61}, the IT-ITeS sector is estimated to have helped create an additional 3 million job opportunities through indirect and induced employment in telecommunications, power, construction, facility management, transportation, catering and other services.

Edward Luce\textsuperscript{62} pointed out that there is an air of optimism and confidence in today’s India which did not exist even a decade ago because with the rapid income growth of the vast Indian middle class is becoming one of the fastest and largest growing consumer societies and market places coveted by much of the developed world’s marketers. Indian cities are experiencing a construction boom with new western-style skyscrapers, shopping malls, entertainment complexes and upscale restaurants, all thronging with eager shoppers and patrons. Even the mobile telephone is ubiquitous even among the lowest of wage earners.


\textsuperscript{62} Uce, E. (2007). In spite of the gods: the strange rise of modern India (1\textsuperscript{st} ed.). Doubleday, 2007.
Dahlman & UTz, 2005 stated that the term “knowledge economy” is increasingly being used in discussions and planning related to development. A knowledge economy “creates, disseminates and uses knowledge to enhance its growth and development. Enhancing the knowledge economy involves developing educated and skilled workers, creating an efficient innovation system and building a dynamic information infrastructure. Thus, for the fruits of India’s economic growth to truly reach a majority of its people, access to knowledge is critical.

Clarence Stone’s study of Atlanta in Regime Politics (1989) is the seminal work laying out this theory. By adopting a political economy approach, it moves the study of local politics beyond the pluralist-elitist debate. While retaining a critical distance from rational choice theory, Stone finds the problem of collective action to be centrally important. The local government condition is one of weak and diffuse authority and this situation favors any group that can act cohesively and control a substantial body of resources. Those endowed with a capacity to promote cooperation can attract allies and overcome oppositional forces. This paradigm offers a broad explanatory framework that assigns central importance to the informal processes of collaboration between those who control investment capital and those who control government authority.

Urban regime theory has become the dominant paradigm in the field of urban politics and policy for more than a decade.

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64 Clarence Stone’s study of Atlanta in Regime Politics
Goetz, 1994\textsuperscript{65} explained that “Political entrepreneurs” were crucial in establishing constituencies that allowed development policies to move forward. Therefore, economic rationality, by itself, cannot adequately explain development policy. Clearly, political forces must be involved and economic development policy is not deterministic.

Pagano and Bowman (1997)\textsuperscript{66} in their study of ten medium sized cities demonstrate the critical role played by civic leaders in molding a community’s future and in forging coalitions to ensure success. Community leaders, as a group share a collective vision of what the city could or should become. In pursuit of this vision, communities mobilize public capital. They explain that they do this in an effort to move the city forward to a desired state. The contended that market failures do not explain why city governments get involved in economic development rather governments intervene in response to changing fiscal conditions and political leaders’ perceptions of their city’s image and its place in the hierarchy of cities.


Bianchi (2001)\textsuperscript{67} mentioned that the agri-food SME clusters have been developed based on strong horizontal relations between members, which analysts link to the delivery of high quality, value added products to end consumers.

Chorda et al., (2002)\textsuperscript{68} pointed out that the major constraints in the competitiveness of SMEs are access to adequate technologies, excessive costs of product development projects, a lack of effective selling techniques and limited market research.

Salaron et al., (2003)\textsuperscript{69} identified that there is an entrance of large multinational processing and retailing firms into the domestic market, changing drastically the infrastructure of food markets and distributed channels.

Carson et al., (2004)\textsuperscript{70} revealed that the overall strength of inter firm relations can indeed play a role in improving the marketing performance of SME cluster.


Narula (2004)\textsuperscript{71} mentioned that an inability to meet the demand for multiple technological competencies, information gaps between marketing and production functions and lack of funds for implementing software such as ERP system are the main constraints of SMEs.

Lal (2004)\textsuperscript{72} found that users of advanced e-business technology perform better than non-users in the export market.

Grunert et al., (2005)\textsuperscript{73} emphasized the role of good vertical relations and end users focus for market orientation in value chains.

Singh et al., (2005)\textsuperscript{74} found that the managers of SMEs face major pressures to reduce costs, improve product quality, deliver goods and services on time in India. The Indian SMEs operate generally in an unsupportive environment.

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Shri and Li (2006)\textsuperscript{75} mentioned that the government would support SMEs actively, improve the quality of service for SMEs, create an environment where enterprises could complete fairly and promise to encourage the development of SMEs with more effective policies, especially in the fields of finance and taxation.

Chen (2006)\textsuperscript{76} pointed out that the founders of SMEs did not possess much personal management or financial expertise and they operated with a dearth of talent within the ranks of senior management. The management systems of SMEs also face excessive government interference related to choice of markets.

Rajesh et al., (2010)\textsuperscript{77} found the governments of China and India have launched various promotional schemes for SMEs. Various challenges for SMEs in these countries are similar; however, the rate of growth is different. Indian SMEs give more attention to supplies development, total productive maintenance and the organizations culture. Chinese SMEs pay more attention to relationship management and cost reduction.


Singh et al., (2007)\textsuperscript{78} observed that the automation of processes, market research and welfare of employees are top ranking priorities for investments by organizations in the Indian Auto components sector.

Chrysoula and Angela (2011)\textsuperscript{79} found that the configuration of horizontal relationship between produces SMEs has little bearing on marketing performance, unless also accompanied by strong vertical connection between key members of the SME cluster and other actors in the supply chain. The disposition of these key members towards information – seeking and contact building outside their SME clusters is also identified as important.

Chevassus – Lozza and Galliano (2003)\textsuperscript{80} found that being near a concentration of export firms located in a metropolitan area had a positive impact on a small firm decision or propensity to export.

Chetty and Campbell – Hunt (2003)\textsuperscript{81} found that extensive domestic distribution networks provided the launching pad into international markets.


Chevasrus – Lozza and Galliano (2003) found the most important determinant of a firm’s export behavior was the international experience of the network they belonged to. Further, better business networks, and the cooperative activities that flow from them, could help expand the pool of inter-firm knowledge sharing activities, production sharing and commercial business capabilities among regional exporters.

Katsikeas et al., (2005) identified the importance of location in the determination of export performance of the SMEs. They revealed that there is a significant influence of the location of the SMEs on its export performance.

MacGregor and Varazalic (2005) included the difficulties in attracting investment and accessing finance, recruiting and retaining skilled staffs, dealing with government policies and programmes and establishing and maintaining adequate infrastructure to support the regions.

Boschma (2005)\textsuperscript{85} suggested that the SMEs’ ability to develop resources and capabilities are highly related to their access to networks and the level of infrastructure services to the SMEs.

Belso – Martinez (2006)\textsuperscript{86} mentioned that there is a positive correlation between firms located inside industrial districts with export performance.

Sapienza et al., (2006)\textsuperscript{87} revealed that the firm location influences firm resources and capability development, thus indirectly impacting on a firms export performance,

Dyer and Hatch (2006)\textsuperscript{88} revealed that sharing of information facilitates new product development enabling SMEs to compete more effectively in export markets.

Chmielewski and Paladino (2007)\textsuperscript{89} found that the success or failure of the firm rest on the specific resources available, capabilities developed and the attractiveness or otherwise of the market in which the firm is operating.


Ruppenthal (2009) mentioned the performance of SMEs depend on the characteristics of the industry in which the firm operates.

Ahuja (2000) investigated the relationship between these different types of embeddedness and firm innovation. He revealed that the significant positive impact of embeddedness on the firm’s innovation.

Schmitz (2004) pointed out that Industry clusters are becoming modes in global value chains and specialized in just one phase of the global production process. As a result, really diverse knowledge is outside the cluster boundaries.

Zaheer and Bell (2005) revealed that the higher degree of closure of the firm’s ego–centered knowledge network, the more successful the firm will be.


Boschma (2005)\textsuperscript{94} mentioned a certain degree of network closure can be beneficial for the development of new ideas and products of the firm.

Laursen and Salter (2006)\textsuperscript{95} found that firms that sit on a structural hole are more innovative than other firms. That firms act as a knowledge network brothers.

Giuliani (2007)\textsuperscript{96} revealed that all firms are as embedded or positioned as equally within their respective cluster knowledge networks.

Elisa (2010)\textsuperscript{97} showed that local embeddedness positively influences the development of successful products, but with decreasing returns. More importantly, however, the researcher found that external openness is more significant than local embeddedness for explaining firm success.

Chiarvesio et al., (2010)\textsuperscript{98} identified that there is a relationship between extra cluster linkages and innovation, or other performance indicators.


Edgardo et al., (2013)\textsuperscript{99} observed that the sustainability indicators framework can be adopted from international structures to the local / regional situation. When companies have framed their performance under international certifications allowing to count with a minimum of indicators to be used for sustainable development – tracking.

Filipovic.F\textsuperscript{100} stated that “In an entrepreneurial economy cluster is defined as the mutual interaction of several related groups or affiliations within a certain social activity. The term itself represents a process of grouping, in the shape of grapes, which in economic sense presents collectiveness of economic, business or others subjects with the mutual goal. European Commission\textsuperscript{101} studied that In “Cluster history” special attention was given to cultural and social factors which influence growth and development of economic subjects. It is believed that non-economic factors represent essential environment for regional cluster development. The focus on four approaches of interpreting regional cluster development and they are industrial districts, The Californian School, The Nordic School and Porter’s industrial cluster.


\textsuperscript{100} Filipovic, F. (editor): Englesko-hrvatski rjecnik, Skolska Knjiga, p. 190.

\textsuperscript{101} European Commission, Observatory of European SMEs, Regional Cluster in Europe, p. 13-14
According to the World Tourism Organization (WTO, 2004)\textsuperscript{102}, tourism is a sector that favors local development because it generates jobs, increases the income of workers and stimulates capital investments through new business opportunities, which results in the establishment of new organizations, including SME, among other advantages. The development of tourism can also bring many negative impacts to the economic, social and environmental sustainability of the local community, such as noise, water and visual pollution, invasion of protected areas, property speculation, increased violence, loss of local identity and culture, modification of consumer patterns etc.

To Zacarelli (2004, p. 200)\textsuperscript{103}, a complete cluster must include some other technology-related characteristics as well as characteristics related to competitiveness, environmental and cultural sustainability, quality of life and synergy as a result of systemic relations. The variables presented, Porter adds: the habit of reusing recyclable materials or sub-products; intense competition among cluster actors and from them to other clusters; similar technological pattern among enterprises; society culture adapted to cluster activities; high correlation and synergy among activities, agents and widening benefits concerning quality of living.


Beni, (2003, p. 74)\textsuperscript{104} highlighted that the tourism cluster is a group of highlighted tourism attractions within a limited geographic space provided with high quality equipment and services, social and political cohesion, linkage between productive chain and associative culture, and excellent management in company nets that bring about comparative and competitive strategic advantages.

M.E. Porter\textsuperscript{105} quotes that “grapes” are result of concentration mutual connected companies and institutions and that they represent new way of business thinking and business philosophy.

According to Montfort (2000, p. 46)\textsuperscript{106} the tourism cluster concept, “A complex group of different elements, including services carried out by tourism companies or business (lodging, restoration, travel agencies, aquatic and theme parks, etc...); richness provided by tourist holiday experiences; multidimensional gathering of interrelated companies and industries; communication and transportation infrastructures; complementary activities (commercial allotment, holiday traditions, etc.); supporting services (formation and information, etc); and natural resources and institutional policies.

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\textsuperscript{105} Porter, M.: Clusters and the New Ekonomic of Competition, Harvard Business Review, USA, p. 85
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Smith, (1989)\textsuperscript{107} stated that a region that is suitable for the development of tourism should have cultural, physical-natural and social characteristics that define its identity, accessibility to infrastructure, supra-structure (accommodation, restaurants., transport, etc.) to guarantee high quality tourism, strategic location near places where tourists come from, enough tourist attractions to draw tourists and sustainable economic activity. There should also be good tourism marketing strategies in order to divulge an attractive, unique and competitive image of its tourism product.

According to P. Andriani (2005)\textsuperscript{108} Existing experience of clusterization indicates that the most effective clusters have evolved evolutionally, engaging related and complement industries in its structure, including businesses which are capable of competition and cooperation at the same time – thereby increase in manufactured products’ quality and cost reduction are caused by the agglomeration effects. But synergy, which is inherent in “naturally grown” industrial structures, cannot be observed in case the enterprises are grouped under the overall resources and strategic basis within the implementation of “the state cluster policy concept”.


By M. Porter (2009)\textsuperscript{109}, cluster is a “geographic concentration of interconnected businesses, suppliers, and associated institutions in a particular field”, which is “considered to increase the productivity with which companies can compete, nationally and globally”.

M.K. Romanova (2011)\textsuperscript{110} concludes the positive nature of clusterization from its most fundamental feature – being a vehicle for a maintaining diversity and overcoming the inward focus, inertia, inflexibility, and accommodation among rivals that slows or blocks competitive upgrading. However, for the positive externalities to arise, it is necessary to gather a critical mass of business and social organizations within the cluster. Another important phenomenon is an informational or technological spillover, as it influences a lot on the processes of agglomeration and convergence – in a positive, as well as in a negative way, leading to standardization and unification of technological base and a lower level of competition.


E.G. Popkova et al., (2010)\textsuperscript{111} stated that a strong cluster suppresses the enterprises, which remain beyond the borders of cluster infrastructure, taking away their market shares due to the essential advantages in costs and product innovations. There is little doubt that such outsiders are represented by small and medium enterprises (so-called SMEs), not to mention micro-businesses, which are hardly to survive in such a “neighbourhood”. It may be attributed to the concept of cluster policy in Russia: it is focused undoubtedly on the introduction and modernization of advanced technologies, while only large-scale business can afford the elaboration and application of R&D, to a considerable extent.

In India, it is estimated that there are approximately 350 Small Scale Industries (SSI) clusters and around 2000 rural and artisan based clusters contributing to almost 60% of the manufactured exports and 40% of the employment in the manufacturing industry. These clusters have been in existence in India for several decades and sometimes even for centuries (Gulati, 1996)\textsuperscript{112}.

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\textsuperscript{111} E.G. Popkova et al., Economic growth in the context of developing economies, Proceedings of the conference Problems of development of worldwide economy in after crisis period, Graduate School of Management, France, (2010), 75-80.
\textsuperscript{112} Gulati M., 1997, Restructuring and Modernizing SSI clusters, UNIDO Report.
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Ceglie, Dini, Clara, UNIDO (1999)\textsuperscript{113} stated that some of the main obstacles hampering cluster development are the following:

- the lack of a cultural attitude towards cooperation both at the firm and at the institutional level;
- the significance of the transaction costs that need to be borne to identify suitable network partners and to forge relationships;
- the absence of incentives (i.e. financial, fiscal, etc.) to the implementation of common projects;
- The imperfect market functioning for the provision of crucial inputs for networking development such as information and innovation; and
- The high risk of “free riding” that is especially faced in contexts where the legal framework to back up joint endeavours is relatively underdeveloped.

A team of Indian consultants, who later became the UNIDO Focal Point of the programme, conducted these studies through interviews with local firms, producers associations, public sector agencies and research institutions. They mapped out existing business practices, inter-firm relationships and the structure of production in each selected cluster. Their study identified the nature and role of institutional support and market linkages available to SSI in each cluster.

\textsuperscript{113} Ceglie, G., Dini, M., Clara, M., 1999, SME Cluster Network Development in Developing Countries: the Experience of UNIDO, UNIDO Report.
It also outlined the main issues raised by firms regarding the problems and opportunities they faced in their particular sector (Tewari, 1997)\textsuperscript{114}.

Industrial clusters are defined as the concentration of economic activities of a certain sector in a certain location producing similar and closely related goods. Industrial clusters include not only the concentration of output producing enterprises, but also input suppliers, output buyers, various service providers and in some cases government and non-governmental institutions. Industrial clusters provide a wide range of advantages that enable enterprises to become competitive and profitable (Schmitz and Nadvi, 1999)\textsuperscript{115}.

Besides promoting existing natural clusters, cluster development policies may involve establishing clusters from scratch with the aim of duplicating successful clusters in regions that lack the basis for natural clusters, especially in lagging peripheral regions of developing countries. Although these types of cluster policies are not common, they exist in certain countries such as the cluster-based industrial parks in Senegal and Liberia (Monga, 2011)\textsuperscript{116}.

\textsuperscript{114} Tewari, M., 1997, Supporting SME Production Networks: some Methodological Themes, Issues and Questions, UNIDO internal report.


The level of specialization and inter-firm linkages in government created clusters is not as high as that of natural clusters. The functional elements of clustering such as trust, collaboration and tacit flow of knowledge that are often present in natural clusters are also absent in government created clusters. This is because it takes a longer period of time for the functional elements of clustering to develop. Physical closeness alone is neither a necessary nor a sufficient condition for inter-firm linkages and spillovers that are held to be key cluster features, to occur (Boschma, 2005)\textsuperscript{117}.

Cumbers and MacKinnon (2004, p. 960)\textsuperscript{118} stated that what is the added value of the cluster approach to existing theories of agglomeration?“ It seems clear that our definition – and that of most, but not all, others - incorporates traditional agglomeration economies.

Gordon and McCann\textsuperscript{119} note: There is nothing inherently spatial about the social-network model although it has explicit spatial applications. This is because social networks are a form of durable social capital, created (and maintained) through a combination of social history and ongoing collective action. In this sense, their strength is inherently problematic, depending upon a prior accumulation of trust,


circumstances which facilitate monitoring of others’ behavior, a source of leadership and/or a sense of common interest... Many of these preconditions are made possible by propinquity, particularly where economic relations have historically been more localized and/or there is a distinctive local economic base and cultural or personal links among key actors. (p. 520)

As Porter notes (2000)\textsuperscript{120}, “the mere presence of firms, suppliers, and institutions in a location creates the potential for economic value, but it does not necessarily ensure the realization of this potential... Many of the competitive advantage of clusters depend on the free flow of information, the discovery of value-adding exchanges or transactions, the willingness to align agendas and to work across organizations, and strong motivations for improvement” (p. 264).

Gordon and McCann (2000, p.521)\textsuperscript{121} cite Granovetter (1973) whose research showed that networks with weak ties, “characterized by pluralistic and open-ended network building strategies in which actors cultivate more extensive sets of links” are more likely to produce innovation than strong and tight ties among a smaller number of like-minded people.


As Porter notes (2000, p.254)\textsuperscript{122} says, “Most clusters include: end-product or service companies; suppliers of specialized inputs, components, machinery, and services; financial institutions; and firms in related industries. Clusters also often include firms in downstream industries (channels or customers); producers of complementary products; and specialized infrastructure providers. Clusters also include a number of institutions, governmental or otherwise, that provide specialized training, education, information, research, and technical support (universities, think tanks, vocational training providers); and standards setting agencies. Government departments and regulatory agencies....can be considered part of it. Finally many clusters include trade associations and other collective sector bodies that support cluster members.”

Porter (2003)\textsuperscript{123} observes, “A major constraint to the analysis of clusters has been the lack of a systematic approach to defining the industries that should be included in each cluster and the absence of consistent empirical data on cluster composition across a large sample of regional economies” (p. 562).


Duranton and Puga (2004, p. 2098) observe that a fundamental feature of learning is that in many (if not most) cases, it is not a solitary activity taking place in a void. Instead, it involves interactions with others and many of these interactions have a ‘face-to-face’ nature. Cities, by bringing together a large number of people, may thus facilitate learning… Moreover, the advantages of cities for learning regard not only cutting-edge technologies, but also the acquisition of skills and ‘everyday’ incremental knowledge creation, diffusion, and accumulation.

Enright (2003) characterizes clusters along various dimensions: geographic scope, density, breadth (range of horizontally related industries), depth (range of vertically related industries), activity base, geographic span of sales, strength of competitive position, stage of development, nature of the technological activities, innovative capacity, and ownership structure. He also uses several categories to characterize the state of development of clusters: working clusters, latent clusters, potential clusters, policy driven clusters (chosen by government to support, but that lack a critical mass of firms), and “wishful thinking clusters” (lacking a mass of firms and any source of advantage).


Clusters from developing countries usually encounter difficulties to achieve the critical mass of firms needed to create sizeable learning externalities to enable the further development of the cluster. This is especially applicable to most African countries, according to Bennell (1998)\textsuperscript{126}.

The linkages between cluster actors (firms, government, academia, finance and institutions for collaboration) are generally less developed in non-industrialized countries. Therefore, greater flexibility regarding the level of linkage development is necessary when analysing clusters from less-developed economies, where emerging and developing clusters are predominant. The more pronounced weaknesses of SMEs and the less frequent interactions between cluster agents in developing countries – in comparison with developed ones – represent severe obstacles to cluster development. (Anderson et al., 2004)\textsuperscript{127}.

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