Iranian Government Globalization Policy Impacts on SMEs and the Corresponding Effect on Iranian-Swedish Trade

By Tony Zohari
Acknowledgement:
I would like to take this opportunity to extend my appreciation to the following institutions and people;

I would like to thank the Iranian National Center for Globalization Studies, the Swedish Trade Council, Swedish embassy in Tehran, Stockholm University School of Business and all other organisations and individuals that has supported me and contributed to this study. In addition I will thank Professor Sten Söderman my supervisor for his enormous support and guideline through the whole study as it would be almost impossible to complete this paper without his guideline. I wish, furthermore to thank Professor Amjad Hadjikani from Uppsala University and Mr Reza Khelili-Dylami from Swedish Parliament for their valuable suggestions and guideline.

Tony Zohari
Stockholm, 01 Jun. 08

Foreword:
Chapter 1 of this paper introduce the background and the purpose of study, Chapter 2 describes the method and the framework I have used to conduct the research. However as I have assumed that many readers of this paper may not be familiar with the current situation in Iran I have added further background of the country in Chapter 3. Chapter 3 may feel not directly related to the purpose of the study however I thought that would be essential to understand the current situation in Iran in order to analyse SMEs environment. Chapter 4 presents the theories I have used in the research and remaining Chapters 5, 6 and 7 presents the data and analyse of the research.
Abstract:
Macro-environmental elements have a vital impact on companies. Traditionally, the government in most countries plays a significant rule in shaping the macro-environment of the country. Therefore, various government policies and programmes are important for managers in analyse of the future threats and/or opportunities of the market. This paper investigating in Iranian globalization policy impacts on SMEs environment and international trade.

Purpose- The purpose of this paper is to describe the impact of Iranian globalization policy on the SMEs environment and the corresponding effect on Iranian-Swedish trade.

Methodology/design/approach- This study has focused on SMEs environment in Iran. The research has been conducted through desk research and semi-structured interviews with fairly open framework with senior management of 13 Swedish and Iranian SMEs all active in Iranian market with international trade. The research is based on theories in relation to PEST analyse, the Uppsala Internationalization Model and Export Modes and Intermediate Entry Modes. A qualitative approach was used as the study focus on the management perception and motivation in the internationalization process.

Findings- The data has shown that the country high political risk has been the main barriers to international trade. However weak management capacities, low labour productivity and failure of government implementation of its policy had had a major impact on trade reduction and SMEs environment.

Keywords- SMEs, Globalization, Iran, Government policy, and Macro-Environment
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"The children of Adam are limbs of each other
Having been created of one essence.
When the calamity of time afflicts one limb
The other limbs cannot remain at rest.
If thou hast no sympathy for the troubles of others
Thou art unworthy to be called by the name of a man."

Saadi
Chapter 1: Introduction

1.1 Background of the Study

Small and Medium-sized Enterprises (SMEs) have played a significant role in the economic development of most countries, especially in the case of Iran, because SMEs make up the majority of manufacturing enterprises. Moreover, approximately 75 percent of them are small businesses that have between 10-49 employees. More than 63 percent of total Iranian manpower in the industrial sector are employed by SMEs, and the share of SMEs in value amounts to approximately 30 percent, and, in total, represents 99.9 percent of all businesses in Iran.

Figure 1.1

<table>
<thead>
<tr>
<th>Business Sector</th>
<th>1-5 employees</th>
<th>6-9 employees</th>
<th>10-49 employees</th>
<th>50-99 employees</th>
<th>&lt;100 employees</th>
</tr>
</thead>
<tbody>
<tr>
<td>Services</td>
<td>878.774</td>
<td>5.031</td>
<td>3.476</td>
<td>231</td>
<td>150</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>334.030</td>
<td>17.126</td>
<td>13.236</td>
<td>1056</td>
<td>1207</td>
</tr>
<tr>
<td>Mining</td>
<td>454</td>
<td>355</td>
<td>413</td>
<td>NA</td>
<td>NA</td>
</tr>
<tr>
<td>Totals</td>
<td>1,213.858</td>
<td>23.111</td>
<td>17.127</td>
<td>1,286</td>
<td>1,357</td>
</tr>
<tr>
<td>Percent of total</td>
<td>96.6%</td>
<td>1.8%</td>
<td>1.4%</td>
<td>0.1%</td>
<td>0.1%</td>
</tr>
</tbody>
</table>

Source: Statistical Yearbook of Iran 1375 (1996/1997)
Note: 1 Manufacturing enterprises with 1-5 employees are mostly artisanal firms, like tailors, bakers, repair shops, plumbers, hairdressers, etc.

However, little is known about the effects of globalization on the performance of SMEs, (Covin and Slevin, 1991; McDougall and Oviatt, 1996; Coviello and McAuley, 1999). Although potential benefits of globalization for Iranian SMEs could be immense, very few of them have been able to substantially benefit from international trade due to both external and internal constraints. The facts show that Iran has not been able to increase its share in international trade despite the preferential market access opportunities provided by its neighbouring countries through The Economic Cooperation Organization (ECO). Referring to the Head of Iran Chamber of Commerce, Iran is ranked as the 18th regional country in terms of growth in production. Furthermore, according to the World Bank (WB) report, Iran's annual

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5 Mohammad Nahavandian, Head of Iran Chamber of Commerce, Source IRNA, http://www.irna.com/ 02 Feb 2007
economic growth in 2006 stood at 4.3 percent, showing a slim decline compared to 4.6 percent\(^6\) in 2005, which stood well below the region's average growth.

Adversely, if you look at the situation from the Swedish viewpoint, the trade relation between Iran and Sweden has become weaker during recent years. Referring to statistics from the Swedish Trade Council\(^7\), Swedish exports to Iran have decreased from 7.8 billion SEK in 2005 to 2.3 billion SEK in 2007. At first glance, this reduction may seem to be due to the UN\(^8\)'s imposed economic sanctions against Iran. However, a more cautious study of the statistics show that this reduction has been far more than expected. In fact, there has been a remarkable decrease in the industries which are not even the subject of the sanction, e.g. food, raw materials, chemical products, semi-manufactures paper and board, tools, agricultural machinery, passenger cars and more. On the other hand, when referring to the statistical centre of Iran\(^9\) (SCI), Iran's imports have increased by more than 12 percent annually during the same period. The biggest Iranian import partners have been Germany, China and United Arab Emirates (UAE). EU's countries on average have increased their exports to Iran by 8 percent during this period, referring to European Commission\(^10\) (EC).

1.2 Problem Area

There are those who do not support globalization and believe Iran is not ready for the integration into the global economy. However, the fact is that globalization is here to stay and if we do not embrace this thought we may get regret it later. With the development of so much new technology, international trade has become more common than ever and it affects everyone's life on a daily basis. This can be realised just by walking to the local grocery in Tehran and counting the number of foreign items on the display. However, since Iran has officially been insulated from the global economy for many years, the new challenge for Iran is how to adjust its economic structure to enhance global integration. Iran also must achieve sustainable development and create competitive advantages in the globalized world of rapid technological change, driven by inequalities of wealth and power.

SMEs have played the dominant rule in Iran's economy with minimal influence over the economic policymaking of the country. However, the SME environment has not been of great interest for the academic discipline due to the characteristics of SMEs and the

\(^6\) http://www.presstv.ir/ 10 Jan 2008
\(^7\) http://www.tradeprofiles.swedishtrade.se/default.asp?id=55  22 March 2008
\(^8\) http://www.un.org/english/ 23 March 2008
difficulty to generalize the findings of any research. As a result, there is a lack of empirical research about the performance of SMEs and the likely impact of globalization on Iranian SMEs which this research is intended to overcome and contribute to the field of study.

As a part of the Iranian economic structure adjustment programme, the government has adopted globalization policies (appendix 4) in order to maximize the benefits to industry and minimize the barriers to SME development (appendix 5) in Iran during the process of global integration and the membership of the World Trade Organization (WTO). While talking about global integration, we must understand that Iran's national economy has not even internally integrated. Market institutions and forces have yet to emerge in a competitive way. More than 19 percent of its population lives in poverty and illiteracy is rampant. More than 33 percent of the population earns their livelihood from agriculture, which constitutes a mere 26 percent of Iran’s national income, which represents 26 percent of non-oil exports. However, the main objective of Iran’s 4th Five Year Development Plan (2005-2009) has been to achieve fast, sustainable growth relying on the transition to a market economy, trade liberalization and privatization. My hypothesis is that the change of government policy and regulations have affected the business environment in Iran and has created new business buyer behaviour.

Figure 1.2:1: Policy impact on SMEs

The new market economy and business behaviour in Iran has impacted international trade and could be one of the contributing causes to the decrease of Swedish exports to Iran. Due to notable decrease of Swedish trade with Iran, I am particularly interested to look at the various export modes used by Swedish companies in Iran to investigate the potential change of strategy and adaptation to the new market economy and business environment in Iran.

1.3 Purpose of the Study
Macro-environmental elements have a vital impact on companies. Traditionally, the government in most countries plays a significant rule in shaping the macro-environment

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12 Ibid
13 Ibid
of the country. Therefore, various government policies and programmes, such as industrial policy, labour policy, financial and fiscal policy, trade policy, foreign policy, education and training programmes and technology policy are important for managers in the analysis of the future threats and/or opportunities of the market. However, the purpose of this study is to describe the impact of Iranian globalization policy on the SMEs environment and the corresponding effect on Iranian-Swedish trade. In addition, I will examine various decisive factors affecting Swedish companies'/investors' decision for increasing commitments/investments in the Iranian market to elucidate the most important criteria for Foreign Direct Investment (FDI) in Iran.
Chapter 2: Methodology

2.1 Research Questions
As result of the new government globalization policy in 2006 and the 4th Five Year Development Plan (Appendix: 4)

- What has been the impact of the Iranian globalization policy on the SME environment?
- How has the adaptation of new government policies affected international trade with Iran?
- What have been the barriers and causes behind Sweden’s trade reduction with Iran?

2.2 Analysis of the Questions
My intention was to find out the various factors that changed between 2005-2008 in Iran’s macro-environment that affected international trade. I looked at three most dominated macro-environmental factors (Appendix 1):

A. Economic
B. Socio-cultural
C. Political

In early stage of the study, I realized that the socio-cultural environment in Iran has not significantly changed during the afore-mentioned period, so I decided not to focus on this factor. My decision was not based on the fact that the socio-cultural factor is not important for the business, but because as it has been unchanged, it is partly irrelevant for the purposes of this study. From two remaining environments, economic and political, 12 additional questions (Appendix 1) were developed as a guideline during semi-structured interviews. However, the questions were not used in a specific order during the interviews, sometimes they varied depending on the respondent's answers, personal background and the company. Questions 1-9 were occasionally presented with some alternatives to help the respondent, however questions 10-12, which were the main part of interviews, were presented open-ended and unstructured so the respondent could discuss and explain their point of view about the phenomena. This enabled me to elicit as much information as possible.
2.3 General method of Study

For the secondary source, I used the Internet, published reports and newspaper articles. The nature of the report, as a result, will be descriptive. For the purpose of hypothesis testing, I used a series of interviews as a primary data source.

2.3.1 Deductive or Inductive

As I have already acquired some facts through observation, desk research and some informal and unstructured interviews, I developed my hypothesis using inductive reasoning, which I intended to test with this study. I came to a decision to use only deductive reasoning to expand the relation between hypothesis and its empiricism.\(^{14}\) As we can see from the deductive process shown below, even the data collection is going to be controlled by hypothesis, meaning I collected only relevant data to confirm or reject the hypothesis.

1. Theory
2. Hypothesis
3. Collection of data
4. Results
5. Hypothesis confirmed or rejected
6. Re-drafting theories

Deductive process (Bryman, 2005)

2.3.2 Positivism Vs Hermeneutics

Positivism and hermeneutics are theories and philosophical frameworks for the creation and understanding of science. Positivism, the most prominent and dominating ideology during the 1900s, inherited its name from the theories of Auguste Comte. It builds on the assumption that even the social science study should be based on the general natural scientific models to develop its theory and understanding of the concept. Alternatively, hermeneutics, which means interpretation of text, was called anti-positivism until the early 1900s. It is a theoretical framework which is based on the idea that it is not enough to conduct a social science study based on existing natural science models, and that a sociological study must include symbolic values (qualitative/non-quantitative) and therefore cannot employ the natural science model.\(^{15}\)

As I try to understand and interpret the Iranian government globalization policy’s impact on SMEs in its existing context, without reducing vital non-material components, I have decided to use the hermeneutics framework for this study. This is because I believe social science cannot be explicated with a simplified reality and that social phenomenon should be studied in its original context.

\(^{15}\) Andersson S (1979) Positivism Vs hermeneutic, bokförlaget Korpen
2.3.3 Quantitative or Qualitative
Now, let's look back to the research questions, as their objective is to measure Iranian globalization policy impacts on SMEs and how this affects the business environment and buying behaviours. Being outcome-oriented and focused on management behaviour, we know the qualitative method is an appropriate way to study behaviours, evaluate feeling, perception, motivation and all other phenomenon related to human mind\(^{16}\). Therefore, I have come to the conclusion that I will use a qualitative strategy for this research.

2.3.4 Literature Review
At first I reviewed books, printed material and academic journals referring to the globalization phenomenon and buyer behaviours from the international relations, business and marketing academic disciplines. In addition, I looked at Iranian Constitutional law from 1979, the 4\(^{th}\) Five Year Development Plan (2005-2009) and Iranian Globalization policy from 2006. Then, I collected data and information from news and professional/industries reports over the Internet related to the topic and information provided through the interviews.

2.3.4 Sample Selection
From a list of 112 Swedish companies in Iran provided by embassy of Sweden, I interviewed seven Iranian and six Swedish SMEs business managers from various sectors in Iranian market. The companies were randomly selected from agricultural, service and manufactory industries in order to create better representative for the whole SMEs environment. Moreover, I chose to also interview one Swedish and one Iranian manager from LSEs\(^{17}\) to find out if they had the same experience about the Iranian market as SMEs managers and how their trade has been affected during the same period. Some of the SMEs managers were interviewed more than one time to establish a better understanding referring to their industry and situation. All of the managers were at the senior level, e.g. managing director or sales and marketing directors. I also interviewed seven experts referring to Iranian affairs, such as a university professor who specializes in the subject as well as Iran, the Swedish trade council, a member of Swedish parliament, Swedish embassy and Nordea Bank.

2.4 Primary Data Collection

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\(^{16}\) Bryman A, (2001) Social Research Methods, Oxford University Press,

\(^{17}\) Large-scale enterprises
The main tool to collect primary data was interviews. However, some facts were collected through observation during my 40-day visit in Tehran in 2007. Data was collected referring to market situation, management behaviour, tax regulation, distribution channel, advertising regulation and people perceptions and managers opinion in the industries.

2.5 Interview Methods
During my travel to Tehran, I visited many companies and had unstructured, face to face interviews with the management. This helped me to develop a better understanding about the market situation and design more detailed and relevant questions referring to the phenomenon. Those questions were then used for a semi-structured telephone interview. Most participants received an email from me before the telephone interviews, which included some background information about the topic, problems investigated and the purpose of the study. The telephone interviews were pre-arranged with participants.

2.6 Definition of term SMEs
In 2003, the European Commission18 adopted a new recommendation regarding the SME definition, which replaced the old one. According to the new definition, an enterprise is “any entity engaged in an economic activity, irrespective of its legal form.” The new recommendation set the following three criteria to determine whether an enterprise is a micro, small or medium-sized enterprise:

- Staff headcount, employ fewer than 250 persons
- Annual turnover, not exceeding 50 million euro
- Annual balance sheet, total not exceeding 43 million euro

It is necessary to note that while it is compulsory to respect the staff headcount thresholds, an SME may choose to instead meet either the turnover or balance sheet ceiling. It does not need to satisfy both and may exceed one of them without losing its status. However, this definition does not need to be accepted globally, but in this study, I am using this as a guideline when I refer to SME even thought I am only focus on industrial SMEs.

2.7 Method Critics
As limited interviews were used for the main primary data collection, even though the findings have been scientifically constructive and very interesting, I have tried to minimize speculative perspective it should be careful to have generalize conclusion about the outcome. Also, using the hermeneutics framework has its own limitations, as

sometimes it has been difficult to determine if the impacts have been caused by globalization policy or other factors, keeping in mind that I did not study the phenomenon in isolation of other macro-environmental elements. The main practical problem was that I could not get some government employees to interview referring the government actions taken in order to implement the policy. A general limitation to the study is, even though I have used semi-structured interviews, most of questions were open-ended and participators explained their perceptions and experiences in a way that makes it difficult to replicate the study again in the exact way. During the interview, I tried to minimize my influence over the participants. However, sometimes I had to describe the barriers and the policy I was investigating and present the question with some alternative answers, which may had some influence on the participants.
Chapter 3: Country background

3.1 Government and Politics

Iran has a very complex system combined of modern Islamic theocracy and democracy. The Supreme Leader, who is considered to be the head of state and controls the armed forces, defence and is the main decision maker on all major foreign policy, is elected by a group of 86 clerics that make up the Assembly of Experts. Only clerics can join the Assembly of Experts and they are elected by the Guardian Council. The Guardian Council, which is considered to be one of the most influential bodies in Iran’s political arena, is combined of six theologians and six jurists elected by the Supreme Leader. They have to approve all bills passed by Parliament. In Parliament, 290 members are elected by people every four years and they can introduce and pass laws. However, those laws have to be approved by the Guardian Council. In addition, Parliament can summon and impeach ministers or the president. The President, who is head of the executive branch of power, is elected every four years by the people. However, he/she has to be approved by the Guardian Council before election to be a candidate.

3.2 Demographics

Iran, with a total area of 1.648 million sq km and population of 71 million, is the largest country in the Middle East. With a median age of 25.8, it is considered to be one of the youngest countries in the world and with a population growth rate above 1.4

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percent\textsuperscript{20}, it is one of the most expanding populations. This fact has become quite a challenge for its government as the country suffers from high unemployment. The challenge is not just to create jobs, but to provide this young population with education, health care, social services, entertainment and a sports facility. However, Iran’s cultural ethnicity is not homogeneous as it is combined by Persian (51 percent), Azeri (24 percent), Gilaki and Mazandarani (8 percent), Kurd (7 percent), Arab (3 percent), Lur (2 percent), Baloch (2 percent), Turkmen (2 percent) and another 1 percent of misc. Almost all of them have their own language, however, Farsi is the most common language. This kind of cultural diversity has been challenging for the central government for many years, as some of those ethnicity groups required more local control and even independency from the central government from time to time. However, this diversity can even be very challenging for the marketer, as for many years Iran had been a central planning economy and most international marketers just needed to deal with the central government. As the country transitions to a market economy, even local authority has achieved higher status and more autonomy and much of local trade is regulated by local government and goods being purchased through local contacts.

\begin{figure}[h]
\centering
\includegraphics[width=0.4\textwidth]{population_millions.png}
\caption{Population}
\end{figure}

\begin{figure}[h]
\centering
\includegraphics[width=0.4\textwidth]{population_age_range.png}
\caption{Population Age Range}
\end{figure}

### 3.3 Economy

Despite a great deal of anti-politics compassion of economists who believe that the politics are unfavourable to the ability of policymakers’ desire to implement policies to ensure national economic spaces are competitive in global economy (Kay, A. 2008)\textsuperscript{21},

\begin{itemize}
\item Adrian Kay, Economism and public policy, University of Bristol, UK, 2008
\end{itemize}
Iranian economic policy is still very much politicized. The government’s decisions are not purely based on cost-benefit method, which has raised criticism from some economics professionals that unsophisticated and basic analysis is being used for political purposes in a way that does not always reflect proper economics. With about 19 percent of the population living below the poverty line, the GDP of $599.2 billion, the real growth rate of 4.3 percent, unemployment rate of about 22 percent and inflation rate above 18.5 percent, the country has a very challenging and unstable economical situation. The ex-economy minister of Iran, who was sacked for blaming President Ahmadinejad for the country’s economic crisis, said on April 22, 2008 that the President uses economic populism to attract votes in next year’s presidential polls. This same minister criticized the recent president's economic policies to reduce interest rates and grant more loans to help industries and the poor as it will cause even higher inflation. Many experts believe the official rate of inflation at 18.5 percent is not correct and the real rate is closer to 30 percent. This economy minister is the sixth minister to have resigned or been fired since Mr. Ahmadinejad took office in 2005.

The government has realised through the IMF and the WB guideline that in order to create one million jobs per year, it is required to stabilize the unemployment rate and the country needs to have at least a 6.5 percent growth rate. This will not be possible unless the government investigates to find a way to retain current firms and/or attract new ones. Otherwise, unemployment will increase and tax revenues will decline. Despite the changes in 2002 to make tax regulation simple, Iran still has very complicated tax system. However, Iran still has one of the lowest tax rates in the world, coming in around 6 percent of GDP and contributing only about 25 percent of

Figure: 3.3:1
ECONOMIC GROWTH AND INFLATION

<table>
<thead>
<tr>
<th>Year</th>
<th>Real GDP growth</th>
<th>Consumer price inflation</th>
<th>Actual</th>
<th>Estimated</th>
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<tbody>
<tr>
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<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2004</td>
<td></td>
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SOURCE: Economist Intelligence Unit

22 Davud Danesh-Jafari
Iranian Government Globalization Policy Impacts on SMEs and the Corresponding Effect on Iranian-Swedish Trade

Iran ranks as the 26th EU trading partner and at the moment, has a trade surplus above $26.5 million and foreign exchange reserves of nearly $60 billion. However, as 74 percent of its exports are dependent on oil revenue, many economists are concerned about its future trade and even the IMF has warned them about the wrong government fiscal policy, saying that if they do not correct their policy, Iran will probably face a deficit in a few years time, despite of increased price of oil. However, despite some international political turbulence, Iran has managed to improve its relationship with the IMF and the WB. Also, in order to tackle those internal economy challenges, improvement of business environment and economic competitiveness, the government, referring to Iran’s 4th Five Year Development Plan (2005-2009), has set its fiscal priority to increase the growth rate, promote privatization, trade liberation and increase transparency in their economic system in order to attract more FDI and reduce budget dependency on oil revenue. The economic prosperity is the most important issue close to an Iranian’s heart at the present time. In fact, a 2005 survey even showed the economical question was the main issue for many voters during the presidential election and the winner was the person who promised most economical prosperity. But many critical reformists believe this economic prosperity will not be achievable if it does not follow some political reforms and empowerment of civil society.

In recent years, the Iranian government has realised that the key to its economical progress is improvement in its international relations. It is a fact that the government had, for many years, ignored this problem due to internal ideological conflicts. But lately, improvement of common relations with the Gulf and other neighbouring states has become among the priorities of the Iranian government. In January 2008, Iran's Foreign Minister admired trade ties with Oman during a meeting with the Omani oil

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27 LUNDVALL, Iran – det ekonomiska läget inför det fortsatta sanktionshotet, UD-MENA, Ambassadrapport http://www.exportnytt.swedishtrade.se/?type=exportnews&id=9248 24 April 2008
29 Manouchehr Mottaki
and gas minister\textsuperscript{30}, calling for more joint investments by the two countries\textsuperscript{31} and on April 22, 2008, the head of Iran’s Chamber of commerce had a meeting with his Omani counterpart to discuss the setup of a joint bank and insurance company\textsuperscript{32}. Due to Iran’s geographical location and the size of its population, it has played conventionally an important role in the region’s economy and security by acting as a bridge, connecting a wide area that includes the Persian Gulf, Caspian Sea, Central Asia (ECO), the South Caucasus, the eastern part of the Arab world and the Indian Sub-continent.

3.4. Market Risks

Iran, like any other foreign market, has certain risks for investors. In this portion of my research, I look at the market from a Swedish point of view to evaluate the attractiveness of the country, as there is no general risk assessment that would imply for all. As some say, one man’s loss is another man’s gain. Throughout history, Iran has had a longstanding trade relationship with France, Germany and England, all of which has created a competitive advantage for those countries and increased the risk for competition from those countries for Swedish companies. As many Iranian firms do not observe their foreign partners as a partner with whom they could develop, there is a high degree of mobility to replace their partners with a new competitor (Amid and Hadjikhani, 2005)\textsuperscript{33}. So, because of this, Swedish companies could easily replace the existing suppliers. Language and cultural differences are other factors that can increase the market risk and there are numerous studies showing its affect on the trade and business environment. This is something that companies should consider cautiously when trading cross-culturally. A study done in 2005 by Amid and Hadjikhani\textsuperscript{34} found that even though Iranian business administrative adaptation was low, the cultural differences between Iranian and foreign companies was not remarkable and not many of managers found language to be a barrier. As a result of insufficient information structure in the society, many newcomers have difficulties finding the right distributor or local agent.

3.4.1 Commercial Risks

Due to economical instability and inadequate management, Iran has a high commercial risk. Because the country is suffering from high inflation and exchange rate fluctuation, trading in its local currency is almost impossible. Most foreign traders use USD for

\textsuperscript{30} Mohammad bin Hamad Al-Rumhy
\textsuperscript{31} Mohammad Nahavandian, President of Iran's Chamber of Commerce, Industries and Mines
\textsuperscript{32} Amid, J. & Hadjikhani A. 2005, Trade, Industrialization and the firm in Iran, I.B. Tauris & Co Ltd, pp 149
\textsuperscript{33} Ibid, pp 148
trade with Iran (Euro € becoming more popular), but even fluctuations of USD create a
certain risk. At the moment, the main commercial risk with trading in Iran is (due to UN
economy sanction, this will be discussed in details under the political risk) the difficulty
to obtain export financing through the Export Credits Guarantee Board (EKN). What’s
more is that it can be even more difficult to ensure payment from the export partner if
some problem occurs due to a contract dispute, bankruptcy, fraud and refusal to accept
the goods. Another general problem in Iran has to do with the complicated custom
regulation system, which means that shipment can often be delayed and goods even
damaged through distribution.

3.4.2 Political Risks
The main intention of this study is to look at trade-related policies in Iran and not
foreign and other government policies. However, in today’s political climate it would be
impossible to talk about the business environment in Iran and not mention the UN’s
sanctions against the country. Iran’s nuclear programme has been a major concern of
international community since 2003, when Iran revealed its uranium enrichment
program. Iran has been a member of International Atomic Energy Agency35 (IAEA)
since 1958 and signed a treaty on the Non-Proliferation of Nuclear Weapons36 (NPT).
Referring to the NPT, Iran claims its right to obtain peaceful nuclear energy under the
supervision of IAEA. As a result, many countries suspect that the Iranian nuclear
programme may not be completely peaceful. The IAEA Director General Mohamed
ElBaradei could not assure the international community that the Iranian nuclear activity
existed exclusively for peaceful purposes in his report, which was send to UN Security
Council on March 8, 2006. Therefore, the UN imposed sanctions following the adoption
of resolution 173737 on December 23, 2006 and followed with a tightened sanction on
March 24, 2007 of the adoption of resolution 1747.38 Referring to those resolutions,
Iran has been banned from importing or exporting any arms and military equipment,
any equipment that can be used in the development of their nuclear programme or/and
any dual-use technology. In addition under the paragraph 7 of resolution 1747 “calls
upon all states and international financial institutions not to enter into new commitments
for grants, financial assistance, and concessional loans, to the government of the
Islamic Republic of Iran, except for humanitarian and developmental purposes”, and
under paragraph 2 of the same resolution, imposed a freeze on financial assets of
some individuals and organizations related to the Iranian government until Iran has

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35 http://www.iaea.org 23 April 2008
suspended all enrichment-related and reprocessing activities and start fully cooperating with the IAEA.

As we can see, the UN’s sanctions itself has an enormous negative impact on the Iranian business environment, even though that is not the only incident behind the reason of that Iran is one of the highest political risks in the world today. A series of events occurring in succession from the revelation in 1979, the hostage crisis at the US embassy, US trade embargo on Iran, Iran-Iraq war, government involvement in various terrorist activities39, terrorist support40 in foreign countries, various human rights issues41 and anti-government demonstration42 on October 8, 2007 at Tehran University, all contributes to the current uncertain situation.

In addition to above, even the various Iranian trade-related policy, such as high foreign tariffs on imported goods, confusing and complicated import regulations and trade documentation, and other factors including: high corruption, high unemployment, inflation rate, environmental disaster, political power structure, government and institutional attitude and behaviour, e.g. some buyer/s act dishonest, are some of the important criterion that Swedish Export Credits Guarantee Board43 (Exportkreditnämnden, EKN) looks at in the assessment of the country’s risks.

EKN is a Swedish organization with international cooperation that helps Swedish exporters with insurance and guarantees their export transaction and investment abroad. EKN, in their approach and assessment of a country’s risks, uses a combined economy model and qualitative evaluation of each case. The economy model looks at the macro-economies element of the country, such as the government’s financial situation, trade balance, debt, payment history and etc. From the economic model calculation, EKN passes judgement on 0-7 scale, with seven as the highest risk, and uses this number as basic data for their qualitative evaluation and the final risks assessment. Iran, at the moment, has increased its country’s risks from four in 2006 to six in 2008.44 This higher risk mean that the guarantees would be much more expensive, and in some cases almost impossible, to get a letter of credit from EKN or any Swedish banks for exports to Iran.

40 http://www.state.gov/t/vci/rls/rm/24494.htm, Iranian WMD and Support of Terrorism, Paula A. DeSutter, Assistant Secretary for Verification and Compliance, September 17, 2003
41 http://www.hrw.org/english/docs/2005/01/13/iran9803.htm, 13 Jan 2005
43 http://www.ekn.se, 20 April 2008
44 Bidgol S., Özgün H., and Özgün K., 2006, Risker och Riskbedömning vid handel med Iran, Stockholm University School of Business
Chapter 4: Theory

4.1 Globalization and the Free Trade

The term globalization was first entered into the English dictionary in 1961 (Webster\textsuperscript{45}, 1961: 1965; Schreiter\textsuperscript{46}, 1997). Economists, geographers, journalists and other academics and professionals picked up the concept later during the 1980s. However, the idea of globalization still tends to remain hard to define, as Anthony Giddens observed, “there are few terms that we use so often, but which are in fact as inadequately conceptualized as globalization” (Giddens\textsuperscript{47}, 1996). Persian speakers make a political statement in their choice between the terms 
\textit{Jahanisasi} and 
\textit{Jahanishodan}. The first word, ‘making global’ is associated with a US-led imperialist plan, while the second, ‘becoming global’, embraces connotations of an open process that can be shaped in various future directions (Scholte, 2005).\textsuperscript{48} However, as there is not any general acceptable definition available, it looks like most often, it is described rather than defined. Some people see globalization as internationalization and growth of business transaction between countries and describe this just as an intensified form of international trade. In that sense, advocates believe it brings positive benefits for consumers, helping to increase choice, drive down prices, improve services and generate more jobs and opportunities. But the opponents to internationalization blame this intensified form of international trade for changing the behaviour of consumers and creating a mass consumption and as a result, changing the ecosystem and causing environmental disaster. As an advocate for globalization, I have to say it is of course correct that during recent years, the consumption in developed countries has increased. In my opinion, that is not purely cause of globalization, but is more likely due to mis-education and the wrong cultural perception. Even the environmental degradation is most likely caused by industrialization rather than globalization.\textsuperscript{49}

However, some see globalization as a liberalization of a process of removing authoritatively-imposed controls on movements of resources between countries in order to open the economies and societies around the world.\textsuperscript{50} With this view, the people have more freedom to chose where they want to be or work and again, globalization provides more opportunity. Therefore, it can be seen as a positive force for change that has the potential to raise living standards and drive economies forward.

\textsuperscript{45} Webster (1961) Third New International Dictionary of the English Language Unabridged. Springfield, MA: Merriam
\textsuperscript{48} Jan Aart Scholte, 2005, Globalization a critical introduction, Palgrave Macmillan, 2nd edition
\textsuperscript{49} Wild J, Wild, K and Han J: International Business - the challenges of globalization, Prentice
\textsuperscript{50} Jan Aart Scholte, 2005, Globalization a critical introduction, Palgrave Macmillan, 2nd edition
At the same time, it provides more cultural diversity and gives people a chance to create better understanding about other cultures. It can also cause people to get closer to each other and reduce the risk of wars as well as promote democracy.

It’s important to note, though, that there are some people opposed to globalization who define it as universalization and describe it as a process of standardization and homogenization with world cultural, economic, legal and political convergence\(^{51}\). For example, some economists have even reviewed globalization in terms of the degree to which prices for particular goods and services become the same across countries (Bradford and Lawrence\(^ {52} \), 2004). This is a complete misinterpretation of globalization as it does not actually have anything to do with universalization. By having access to other cultures, personal free will and understanding how other people work does not automatically equal universalization and the process of losing of your own personal identity and culture. On the other hand, we can ask ourselves: is there any culture in the world that has been unchanged through time? Should we stop learning and keep ourselves in isolation just because we do not want changes?

Some critics of globalization believe as the IMF, the WB and the WTO and in general, that wealthier western countries are largely influential in the course of the globalization development\(^ {53} \). They are also seen as the motivating forces behind the policy reforms that the developing countries had to implement as part of their structural adjustment programs under the supervision of the IMF, the World Bank and the WTO\(^ {54} \). Therefore, this group believes that it is obvious that those countries and organizations will only promote their own interests, so they assume globalization is the intensive policy of the industrial western world, particularly of the multinational corporations, to maintain their interest and encourage a new form of colonization; this group defines globalization as westernization. I will not deny that there is some true in the statement above; however as more and more developing countries are applying for membership in those organization, they will be able to influence its policy and shape this process to benefit their development needs. As the head of Iran’s National Center for Research on Globalization\(^ {55} \) says, Tehran should prioritize joining the World Trade Organization to promote their values and interests and at the same time, benefit from the positive development and the opportunities to attract more foreign direct investment.\(^ {56} \)

\(^{51}\) Ibid
\(^{53}\) America Vera-Zavala (2001) global justice is possible, Pocky
\(^{54}\) Ibid
\(^{55}\) http://www.globalization.ir/ , Esfandiar Rahim-Mashael the head of Iran’s National Center for Research on Globalization
\(^{56}\) www.presstv.ir Jan 2008
As most opponents and conditional advocates of globalization are critical to its effect on environmental degradation and other social values which are important to developing societies, they mention that globalization advocates only discuss its positive effect on an economy and ignore other negative effects. I have to agree that the economic policy is not only the core human and social values, and as even the Iranian Constitution has said, the economy is a means, not an end,. But the economy has not been the only force behind globalization either. Globalization is a social scientific phenomenon and the primary problem it was intended to solve was economic, and as most governments have engaged in globalization development policies driven by the idea of economic progress to furnish all citizens with equal and appropriate opportunities. It is also meant to provide them with work, and to satisfy their essential needs, so that the course of their progress may be assured. This can be a good starting point followed by the pursuit of other important concerns such as cultural promotion, ecological care, democracy, peace and etc.

But does the globalization and economic progress help humanity to achieve or improve our values such as ecological care, democracy and peace? To answer this question, we shall define and describe each of those elements separately in details which are clearly beyond the space and scope of this case study. As we all know, economic inequality and poverty has been the basis of most human conflicts. Paul Hirst\(^{57}\) believes that environmental crises will cause a shortage of resources, raw materials, water, dry land and energy, which will produce competing claims for resources, and become the main reason for future conflicts and wars. But even without looking at any social studies and research that has been done on the effects of globalization on the environment, democracy and peace, we can certainly claim that globalization and economic progress will help and has helped to improve the standard of living and so many of those values that are vital to us. And although the discourse on globalization and sustainable development is not homogeneous, most people will agree that it will be easier to overcome future global challenges with international cooperation rather than segregation, no matter what the challenges will be. However as the intention of this study is to investigate the globalization impacts on SMEs and focus mainly on macro economical effects, for the simplicity’s sake, whenever I use the term globalization in this study, I refer to the widely accepted Hollensen\(^{58}\) definition that globalization “reflects the trend of firms buying, developing, producing, selling and distributing

\(^{58}\) Hollensen S. Global marketing, 4th edition 2007, Pearson Education Limited
products and services in most countries and regions of the world" in order to create competitive advantage and increase their market share.

4.2 The World Trade Organization (WTO) and International Monetary Fund (IMF) and the World Bank (WB)

The concept and implementation of those organizations came about during July 1944 at the UN Monetary and Financial Conference in Bretton Woods, New Hampshire. In order to control and develop a global free trade system, three institutions were established: the International Monetary Fund (IMF), the International Bank for Reconstruction and Development (IBRD – also known as the World Bank) and the General Agreement on Tariffs and Trade (GATT -- which was replaced by The World Trade Organization (WTO) in January 1995)

The World Bank is a group of five financial institutions:

1) The International Bank for Reconstruction and Development (IBRD) which Iran become member in 1945
2) The International Development Association (IDA) Iran is member since 1960
3) The International Financial Corporation (IFC) Iran is member since 1956
4) The Multilateral Investment Guarantee Agency (MIGA) Iran is member since 2003
5) The International Centre for Settlement of Investment Disputes (ICSID) Iran is not a member.

The initial purpose of the bank was to aid in the reconstruction of countries damaged by WWII and to control the flow of capital internationally. Since that time, the bank's activity has expanded and its international rule has become even more important. The bank's new mission and goals are poverty reduction globally, strengthening the economies of poor countries, improving living standards, and promoting global economic growth and sustainable development. The WB has a total of 185 member countries, all of which are shareholders and influential in its decision-making process. However, G7 owns about 45 percent of the share and has largest influence over the bank policies. The WB does not give grants normally, but provides loan to the most needy countries under the market rate. At the moment, it has several water supply & sanitation projects, Bam reconstruction project, an urban housing project, Tehran transport emissions reduction project, health care and nutrition project and a smattering of additional projects in Iran.

IMF also has 185 members and Iran is a member with 0.69 percent votes. IMF often collaborates with the WB and was created to “promote international monetary

cooperation, exchange stability, and orderly exchange arrangements; to foster economic growth and high levels of employment; and to provide temporary financial assistance to countries to help ease balance of payments adjustment." However, as of recently, the IMF rule has become more complex, combining to become an international bank, regulator, insurance company and charity. Many anti-globalization activists have criticized the IMF structural adjustment policy in developing countries for creating a larger inequality of wealth.

The WTO, which replaced GATT in 1996, administers the rules governing global trade with six main functions in order to smooth out the progress of international trade with fair and predictable flow of commerce.

1) Making available a forum for trade negotiations among all its members
2) Administering the trade agreements thus negotiated
3) Managing specific trade disputes
4) Monitoring national trade policies
5) Providing technical assistance and training on trade policy for developing countries
6) Cooperating with other international organizations on trade issues

(Moore, & Pubantz, 2006)

The WTO has 151 members and controls almost 90 percent of global trade. Iran applied for membership in 1996, but as the government has not submitted a Memorandum on the Foreign Trade Regime yet, the application is waiting, so at the moment, Iran has an observer place at the WTO. The Iranian membership of the WTO is one of the most challenging and an important fact in the process of globalization for Iran, as the country has been insulated from international economics scene for about 30 years. To become a member, Iran has been required to adjust its economic structure, which has been politically unpopular for the conservative politician. Still, some believe that Iran is not ready for further global integration and in order to protect domestic production, it may be better to wait before getting the full membership.

4.3 Macro-Environmental factors and PEST analyse

A number of external elements in the organizations surroundings have impacts on the organization and effective management decision about their future plan and market strategy. Macro-environmental forces include economic, legal-political, environmental,
socio-cultural and technological elements of each country. Normally, the organizations and their management have minimal influence over macro-environmental elements. Managers collect data and information from the organization surrounding to use for strategic analyse in the way that can help the organization to adjust and adopt itself and its products to its environment in order to create a competitive advantage for the organization.

In order to estimate market potential and the future opportunities or/and threats of the market, management generally uses a PEST model analyse to explain the future market growth or decline. PEST stands for Political, Economic, Socio-cultural and Technological.

4.4 The Uppsala Internationalization Model

Swedish researchers (Johanson and Wiedersheim-Paul, 1975; Johanson and Vahlne, 1977) from Uppsala University had vast criticisms of the theories at the time, which explained international involvement. However, it has been developed as a more independent model to explain the sequential steps in the direction of increased foreign dedication (Johanson & Vahlne, 1977; 1990). They developed their own model of internationalization process based on empirical observation from four Swedish manufacturers and influenced by the works of Penrose (1959), Cyert & March (1963) and Aharoni (1966). The Uppsala Internationalization Model distinguishes four different steps of entering an international market, which cannot be viewed independently of a company’s situation, market and the market knowledge. (See 4.4:1 below)

- Step 1: No regular export activities (sporadic export).
- Step 2: Export via independent representative (export mode).

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Step 3: Establishment of a foreign sales subsidiary.
Step 4: Foreign production/manufacturing.

(Hollensen 2007)

From the observation, they find out that companies normally start their expansion in a nearby market. There, they have better knowledge and control and slowly, when they have acquired better resources, they can expand to market farther away (Faraway market, they do not refer only to the geographical distance; it also includes the differences in language, culture, politics and the difficulty to acquire knowledge and information from the market). Secondly, most often companies entered a new market through export before establishment of foreign sales subsidiary or foreign production.

Figure: 4.4:1 Internationalization of the firm

In their study, they refer to (Aharoni, 1966) about the interdependence of market knowledge and market commitment. They make a distinction between general knowledge and the specific knowledge. The former, which is more about the operation in the foreign market, can easily be transferred from one market to the other. It is important to note that the special knowledge, which is more specific to a particular market, cannot be achieved without specific activity in that market and it would be difficult to use this knowledge in other markets.

4.5 Export Modes and Intermediate Entry Modes

There are many different export modes, however, for the purposes of this study, I concentrate on the three main export modes described by Hollensen as indirect, direct and cooperative export modes. Export is the most common way of entering a foreign market. Indirect export mode is when the manufacturer does not get involved in the exporting activity; they use a domestic broker or export management company to take

care of the foreign sale. Normally, companies use indirect export only when they want to get rid of their surplus production without much expansion strategy to the new market at that moment. This mode been used for many SMEs that do not have the acquired resources to develop their own foreign sales strategy. The second mode, which is direct export, occurs when the manufacturing companies use an agent or a distributor in the foreign market. This has been the most common mode of export to Iran. Lu and Beamish\textsuperscript{67} find that this kind of collaboration with partners with local knowledge can be an effective strategy to overcome the deficiencies SMEs face in resources and capabilities, when they expand into global markets. The final mode is the cooperative export, which is when the manufacturing companies get even more involved in the marketing activity in the host countries. (See figure 3.5:1 below)

![Figure: 4.5:1 Export modes](image)

Source: Svend Hollensen, Global Marketing 2007

4.6 Internationalization Barriers

Hollensen has listed a number of primarily internal barriers that may deter internationalization of the firms;

- Insufficient finances,
- Insufficient knowledge,
- Lack of foreign market connections,
- Lack of export commitment,
- Lack of capital to finance expansion into foreign markets,
- Lack of productive capacity to dedicate to foreign markets,
- Management emphasis on developing domestic markets,
- Cost escalation due to high export manufacturing, distribution and financing expenditures.

(Hollensen, 2007)\textsuperscript{68}

Many of those barriers are stronger for SMEs because of the size of the companies. They often find it more difficult to gather adequate resources to allocate to the various tasks required for expansion into a new market.


\textsuperscript{68} Hollensen S. Global marketing. 4\textsuperscript{th} edition 2007, Pearson Education Limited, pp 53
4.7 SMEs Management Style and its Characteristics

SMEs have been one of the main focuses of study for the entrepreneurship researcher. Even expanding to a new geographic market has fundamentally been considered as an act of entrepreneurship (Burgelman, 1983, Lumpkin and Dess, 1996, Barringer and Greening, 1998). However, SMEs management do not act as a homogeneous group (Julien et al., 1977, Hollensen 2007). Their decision-making is usually spontaneous, flexible and unstructured and as an entrepreneur, their tendency is to seek new opportunities on a regular basis and that may cause radical change in their overall strategy (Hollensen, 2007).

Some general characteristics that most SMEs have in common are financial limitations, as many of them only have access to limited capital through the owner and the owner of the company is usually involved in the management and he/she is the main decision maker. Due to the size of SMEs, most people involved in the business have generalised knowledge and not many of them are specialist or have business education expertise; in fact, they are most often technical or craft experts (Hollensen, 2007).

4.8 Buyer Behaviour

It is not easy to understand why people buy or do not buy a product/brand. Before getting further into the investigation, it would be practical to first look at how people respond to various marketing stimuli and what affects their purchasing process. For...
simplicity purposes, I will use the Buyer Decision Process Model\(^{71}\). This model refers to five stages of the customer’s decision-making process:

1. Need recognition
2. Information search
3. Evaluation of alternatives
4. Purchase decision
5. Post purchase behaviours

\(^{(Kotler, 1996)}\)\(^{72}\)

If there is any interruption at any stage in the process, the buyer may not continue to the next stage and a purchasing decision is never reached. However, to appreciate various stages of this process and how it is being developed, considering the *Stimulus-Response Model of Buyer Behaviours*\(^{73}\) can be helpful. From this model, we can recognize how people will respond to various external stimuli and what role their characteristics play in their final decision. The figure below shows that marketing and other stimuli go into the consumer’s black box and produce certain responses.\(^{74}\) To know what is in the consumer’s black box will help us to understand their responses and behaviour so we can manipulate the stimuli to get the desired outcome.

![Stimulus-Response Model of Buyer Behaviour](image-source)


\(^{73}\) [http://tutor2u.net/business/marketing/buying_stimulus_model.asp](http://tutor2u.net/business/marketing/buying_stimulus_model.asp) 20 March 2008

\(^{74}\) Ibid
Chapter 5 SMEs environment in Iran

5.2 SMEs in Retailing

The retail industry is comprised mainly of small private shops with one to five employees and is managed traditionally by cooperatives and independent retailers with minimal foreign investment operating through urban bazaars. Bazaaris play an important role in Iranian economic policy and the power structure of the country. In 1978, during the Iranian revolution, by calling a series of strikes, detractors immobilized Iran's economic and sped up the removal of the shah. Since then, they have maintained a close connection with the current regime, benefiting from profitable business contracts and tax exception in exchange for funding conservative parliamentary, presidential candidates and mosques. The Bonyad, a grouping of influential religious charity organizations accountable only to Iran's supreme leader, is a key player in retailing, controlling much of the transportation network as well as distribution outlets.

During recent years, the country has seen an increasing number of private single mini-markets and supermarkets and even a few chain stores. The major chain stores are the state-owned Refah, Naft (an offshoot of the Ministry of Oil), Ghods and Sharvand, owned by the Bonyad-e Mostazafan & Janbazan.

Even though no major retailer has established a store in Iran, foreign investment is likely in the near future. Migros Turk, has said that they plan to open an outlet in the Tehran shortly and the Majid Al Futtaim Group LLC, has announced its intention to enter Iran’s market. Fashion retailer Giordano Middle East already has opened a total of 13 stores, seven stores in 2003 and a six more during 2004 and is planning to expand in near future.

The modernization/industrialization program, launched by the Pahlavi regime in the 1960s, was interrupted by the revolution and further by the Iran-Iraq war during 1980's. Even though Iranian consumer goods production has developed in the last three
decades, in general people have maintained a preference for trade over production and demand for consumer goods is still being satisfied largely by imports. For example, the demand for almost two million television sets annually is only met at a rate of 50% by the country’s 14 manufacturers. After the change in Iranian legislation in 2002, stating that foreign companies are now permitted to own more than 49 percent of Iranian companies, some investors have shown more interest and formed local partnerships for production of goods under licensee in order to avoid high import duties on finished goods. A good example of this is Haier\textsuperscript{86}, which produces washing machines & refrigerators. Royal Philips Electronics is to produce 180,000 televisions set a year on the free-trade island of Qeshm through a venture with local partners and LG Group\textsuperscript{87}, which already has a sales subsidiary, is planning to open a manufacturing plant in Iran very soon.\textsuperscript{88}

5.3 SMEs in Agriculture Section

Iran’s agricultural sector accounts for 19 percent of GDP, employs 33 percent of the labour force, represents 26 percent of non-oil exports\textsuperscript{89}, and about 10.2 million hectares of land are cultivated throughout the country. Despite independence in some areas, Iran is one of the world’s largest net importers of agricultural products, importing 20-40 percent of its annual food requirements. In contrast of what most westerners believe, only 20 percent of Iran’s geographical area is desert, the rest is made of natural range land, forest, and roughly 20 percent arable land\textsuperscript{90}. The deficiency in the production is not about availability of land, but rather the shortage of water, outdated machinery, raw material and insufficient farming techniques. Many in the industry believe the problem will not be solved without the influences of the outside world to modernise the industry. Otherwise, the situation will just get worse, particularly when you consider the high growth rate of the population\textsuperscript{91}.

Iranian agriculture problems are not limited to micro-economical factors. It does, in fact, even suffer from macro-economical issues. As part of a recent government economy policy to stabilize the high inflation and control the high prices for food and agricultural goods\textsuperscript{92}, the government has increased imports and caused fluctuation in supply and demand of agricultural goods. This policy has been widely criticized as it has reduced the price of agricultural goods without a significant effect on other goods and inflation.

\textsuperscript{86} http://www.haier.com/ Feb 2008
\textsuperscript{87} http://www.lg.net March 2007
\textsuperscript{88} Business Intelligence, ME, http://www.bi-me.com/main.php?id=311&l=1&c=34&co=
\textsuperscript{90} Business Intelligence, ME, http://www.bi-me.com/main.php?id=311&l=1&c=34&co= 01 Feb 2006
\textsuperscript{91} Ibid
\textsuperscript{92} http://www.voanews.com 12 March 2008
Even the policy to subsidize state-owned farming companies has created unfair competition for small farmers and creates additional barriers for many of them. Those wrong policies have made domestic production unprofitable for SMEs and, as a result, many domestic farmers have been forced to reduce production, which has increased the already high unemployment. Many economists are worrying about this policy’s long-term effect on the nation’s economy and urbanization as it can force many farmers to move to cities in order to find work.

5.4 Manufacturing and Mining SMEs
Petroleum, gas, petrochemical, steel, weaving, food processing, car, electrical and electronics industries are among the key industries in Iran. Due to outdated machinery and insufficient management, except petroleum and gas, not many other Iranian industries have been able to play a significant role in world trade and their production barely satisfies domestic demand. The handicrafts and traditional industries, such as carpets and ceramic industries, are also considered to be key local manufacturers, but even the Persian carpet, which used to be widely welcomed in Western countries, has lost its share of the market to new rivals from Turkey, India, and Pakistan. This is mainly due to wrong export regulation in the early 1980s, which prohibited export and damaged its comparative advantage in its production. Referring to Statistical Centre of Iran (SCI), 93 96.4 percent of all manufacturers are private, while only 3.6 percent belong to the public sector. As the country’s export is mainly dependent on its oil, that 3.6 percent public sector’s companies stand for almost 76 percent of country’s export. This has created great dependency of many industrial SMEs on state-owned LSEs for contracts and the complicated registration for entering into the tender business with LSEs has been a huge barrier for many SMEs. As part of the government privatization plan, in October 2007, Deputy Director of the National Iranian Oil Company announced that a total of 130 oil, gas and petrochemical companies out of 144 would be privatized under a seven-year privatization program.94

In addition, referring to SCI of 3323 operating mines in Iran, 90.2 percent mines are private and 9.8 percent mines are run by public sectors. A total of 55,000 workers are employed by the mining industry95.

5.5 SMEs in Media and Internet

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According to the Iranian Constitution, only the state has the right to own and administrate television and radio. However, with the development of satellite technology, a number of foreign and privately-owned stations from abroad broadcast Persian-language television and radio programs, available for upper and middle class Iranians. The two state-owned media outlets, the Islamic Republic News Agency (IRNA96) and Tehran Times97 are the major news sources from inside of Iran and all 40-50 newspapers and magazines (private or state-owned) rely heavily to them referring to domestic news. And while companies have the right to own and administrate printed newspapers and magazines, all the material used by them has to be controlled by Ministry of Guidance and Islamic Culture98. This policy has been very harmful to SMEs in printed media and the film industry as they have to refer to Ministry of Guidance and Islamic Culture for variety of reasons and as many of them do not have enough resources and bureaucratic skill to negotiate effectively many of them has been out of the business. Due to tough control of print, many Iranians have turned to the Internet for the access of news. This has caused an enormous loss for the print industry and created great benefits for Internet providers, as user rates were raised from 250,000 in 2000 to 19 million in 2006. The Internet is considered to be the main mass communication channel for Iranian youth. Yet, despite the tremendous increase in Internet users, Iranian companies have not been able to take full advantage of it, as research from Luleå University of Technology99 in 2007 found that has been due to deficiencies in payment mechanisms and lack of credit cards, poor distribution logistics, poor telecommunication transmission capability and lack of training.

96 http://www.irna.ir 20 March 2008
99 Ajdari, B. 2007, Impact of e-Commerce on Internationalization of Iranian SMEs, Luleå University of Technology
### Growth and potential of IT in selected countries, 1377 (1998/99)

<table>
<thead>
<tr>
<th>Country</th>
<th>IT Growth Score</th>
<th>Ranking</th>
<th>IT Potential</th>
<th>Ranking</th>
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Source: Industrial Management Institute
Chapter 6 Findings & Analysis

6.1 Responses from various

Of the 12 companies that I asked about how their business and trade has been affected during the last two years in Iran, two of the companies said there have not been significant changes in their business, and three companies said there has actually been improvement in sales. However the remaining seven companies all had been affected negatively and had lost 20-40 percent of trade.

Only one of the companies believed that the increase of import tax on finished goods had an essential impact on their trade reduction. Most other companies said the tax increase had reduced their marginal profit, but a reduction in the trade; they were actually referring to the quantity reduction.

Only one of the Swedish exporters used the cooperative export mode and had its own local office and marketing team. All of the others used the direct export mode through local agents. None of them had significant problems with marketing or distribution activities. Almost all of the companies, with the exceptions of one, had a positive attitude and believed their future trade in Iran would improve within next five years and there would be stronger trade relations between Iran and Sweden.

Referring to Iranian policy to reduce income tax and tax exception in the free trading area in order to improve FDI, all companies said that it has not affected their strategic planning. Only one said that has some positive impact, however they did not have any plans to increase investment in Iran for the near future.

Referring to Iranian government’s 4th Five years development plan, privatization and trade liberation policy, none of the companies believed that it had any noteworthy
impact on the SMEs environment or power structure in Iran. And some believed even if it had some positive effect, it would be neutralized by all other negative impact from other factors which were more influential on SMEs environment in Iran. However most of the companies believed that has been a lack of implementation of the policies and even some referred to it as a policy just on the paper with no reality implication.

All companies, with no hesitation, believed that the UN’s sanctions have had a tremendous negative impact on the Iranian business environment and the trade relations between Iran and Sweden.

Eleven of the companies said that in order to attract FDI in Iran and create a willingness of Swedish investors to invest more in Iran, the most important criterion would be to resolve the political issues. As the country has very high political risks, it would be difficult to attract any investors and some even said that Iranian investors are starting to take their investments abroad. However, only one company said that economical issues are the most important criterion and the commercial risks should be reduced in order to attract FDI.

The three questions “A) From your experience and in your opinion what were/are the major problems and barriers Swedish companies had/have in the trade with Iran? B) What do you think is the reason that Swedish-Iranian trade relations have become weaker in the recent years? C) In your opinion what impact the Iranian privatization, trade liberation, globalization policy and in general recent events had on Iranian SMEs?” were more used as open-ended questions and to allow discussion around the topic. At this point, the respondents could explain their personal experiences and feelings. I even interviewed seven individual experts on Iranian affairs to create a better understanding of the whole picture.

This was the testimony of one of the experts, who had actually come back from Iran the week before the interview and personally had interviewed some Iranian manufacturers. The Iranian economic and business situation has declined the last two years, mainly because of the UN’s sanctions, even though other factors were involved. He said that many of those manufacturers even had difficulties paying their employees as they were lacking raw materials for the production. Therefore, they have had to reduce production, which has caused shortage of sales and liquidity to pay the employees. Alternatively, some of the manufacturers have had to buy the raw material through middlemen, even at times more than one middle man, which makes the material more expensive.
Many companies mentioned say that at present the biggest problem is the difficulty to get L/Cs (Letters of Credit) from any banks or the Swedish Export Credits Guarantee Board (EKN). This means that as a result, they have lost the trade with Iran, even though their product is not the subject of the UN sanction.

Some general issues that have had some impact on trade in Iran referring to some of the companies has been:

- Lack of market knowledge and general knowledge referring to the sanction
- Lack of embassy support, Iranian businessman has difficulty getting a visa
- Lack of interest in the market
- Lack of export & entrepreneurship support from the government
- New competition from China and India
- Lack of financial resources

The Swedish Trade Council’s Consultant\(^{100}\) believed UN sanctions have had a major impact on investments in Iran, as companies feel that the macro-political risks are too high. Long-term investments are avoided as Iran is considered a high risk country by all financial institutions today. However, between 2003 and 2005, Sweden showed high export figures to Iran, but deeper analysis shows that the high export value was based on two major projects, which where finalized in 2006. Siemen’s gas-turbines and Volvo accounted for almost 50 percent of Swedish export to Iran. But, the lack of new business ventures, due to payment restraints between Iranian banks and international banks, have had a large impact. Swedish export companies are not willing to take the payment risks as the Swedish banks no longer are ready to guarantee the risks.

According to the Swedish Ambassador in Iran\(^{101}\), the UN sanctions have been the main reason for the trade reduction between Iran and Sweden. It should be stated that in addition to the sanctions, other factors such as high inflation and high unemployment and the general Iranian economy crisis, played an important role in Sweden’s downplayed role in trade with Iran. The Swedish ambassador referred to statistics and said that recent stats show that Sweden is not the only country to have trade reduction. Even Italy, Germany and some other EU countries have reduced trade in 2008, even though Germany may still play a dominant role in trade with Iran. However, the reason that trade reduction has been larger than estimated is probably where the psychological anxiety about the subject stems from, as Swedish businessmen may be worried about political and social disturbances in Iran. This has

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\(^{100}\) Daniel Mokari, Consultant - Middle East & Eastern Africa, Swedish Trade Council

\(^{101}\) Magnus Wernstedt, Swedish Ambassador in Iran, 2008
magnified the impact of UN sanctions and affected their decision-making to avoid business in Iran as the future economy and business environment in Iran is very uncertain.

In response to the impact of Iranian globalization policy and the 4th five years development plan, the Swedish ambassador replied, “I have been in the country only for a few months so I cannot say much about changes, however, there is still lack of transparency in the government policies and it appears that has not been much improvement or any changes.”

During the interview, I mentioned that some Swedish companies I had interviewed talked about a lack of market knowledge and government support. Then, I asked the ambassador for his views on it and the eventual Swedish government plan. The ambassador responded that Sweden supports the UN’s decisions and follows EU’s policy. However, at the moment, the embassy provides various market researches and some marketing support for Swedish companies in exchange for an agreed-upon fee. But as a result, the Swedish companies interest and request about Iranian market has fallen, embassy does not have any plans for the extended services in that area for the moment. When asked about the future trade between the two countries, the Swedish ambassador was optimistic as he added that Iran needs access to modern technology and training. Since the country has a good financial reserve and Sweden has what Iran needs, a future trade structure would be beneficial for both countries. However, some improvement in Iran’s foreign policy has to come first to dissolve the country’s problem with the international community.

The response to the question referring to the impacts of the Iranian’s globalization policy on the SMEs environment were more speculative as not many of the companies had a direct answer. Three answered that they do not know about its impact on the general SMEs environment, however they did not feel that has any impact on their own business. Four of the companies felt in general the business environment in Iran has gotten more difficult, but they could not say if it was the impact of the globalization policy or other factors or probably a combination of all various factors. Five others said that they did not feel any positive impact or improvement in the SMEs environment and they had even difficulty noticing if the government has implemented any of its policy to overcome the barriers for SMEs.
Three of the managers did point out that high unemployment, high inflation and general economical crises normally hit the SMEs harder. They referred to the difficulty in getting L/Cs and said large companies normally have better financial resources and liquidity so it is easier for them to do business as usual and find other solutions. Many SMEs are dependent on the export/import credit. One of the managers was a sort of conditional advocate of globalization and mentioned the benefit of the Iranian market is that it is isolated at the moment from foreign competition and noted that it’s good that this globalization process is going slowly. This is because many Iranian managers are not trained to operate in the international market and direct competition from abroad may cause many Iranian SMEs to lose their job. He added that Iran must invest in the training and improvement of domestic industries before concentrating on the global market and the market protectionism may be a good strategy for an Iranian SME for the time being.

6.3 Analysis of Responses and Finding

Referring to the Uppsala model, companies follow four different steps of entering an international market, depending on their specific situation, market and market knowledge. A company’s requirements and behaviour varies at different steps in the process. As the Uppsala model looks at the process of internationalization as sequential steps, each step has to fulfill its purpose before the company enters or even considers the next step. The data from Iran shows that currently most Swedish companies are at step two (fig. 6:3.1) in their internationalization process in Iran, and there are only eight Swedish LSEs companies (of 112 companies) using the cooperative export mode. The remaining Swedish companies use the direct export mode through local agents and only two to four Swedish companies of those eight are at steps three and four and have some production facility in Iran. Only one of the Swedish companies included in this study were at step three as I did focus on SME and there were no SMEs, Swedish or Iranian, that had passed step two when it comes to trade between Iran and Sweden.

![Image of Figure 6.3:1: the main export mode to Iran](image-url)
During step two, as most Swedish companies used independent representatives and local agents, it did appear that most Swedish company’s trade was not affected by the higher import tax. As many agents decided not to vary the end price and the higher import tax just caused the agent’s marginal profit to become reduced. (Fig. 6:3.2)

![Figure 6.3:2: the impact of import tax on trade](image)

The higher import tax on the finished goods policy has not had any affect on the increase incentive for Swedish companies to increase their commitment and move from step two to step four. Even though the agents did not keep the end price stable, this policy would not have had any major impact on the decision of Swedish companies to intensify their investment and go from step two to step four (not even to step three). This is because the end price is one of the less important criteria in the decision-making process at this step. On the other hand, those export decisions are more likely to be innovation-oriented instead of problem-oriented (Lee & Brasch, 1978)\(^{102}\). Johanson and Vahlne find that market knowledge is the primary motive behind the commitment decision (fig. 6:3.3) and there is a positive correlation between current activities and market commitment. This model is based on the assumption of the willingness of the firms to increase their long-term profit and that they are also motivated to reduce risks.

![Figure 6.3:3 The Basic Mechanism of Internationalization-State and Change Aspects.](image)


During this study, three of the respondents mentioned a lack of market knowledge and the difficulty to gather sufficient data from the market as one of the problems in Iran. Due to positive correlation between current activities of the firms and its market commitment, it is likely that the policy to limit firms’ current activity will not increase an incentive to increase market commitment as it has more likely opposite effect.

Even by assuming firms’ long-term profitability and risks minimization motive at this stage, even a policy like income tax redaction will not have a major impact on the Swedish firms’ commitment decision. (Fig 6:3.4) At step two, the initial objectives of the firms are sales maximization and market knowledge acquirement. Having tax reduction in the host country did not affect their commitment because the short-term profit maximization is not a criteria on their priority list in the process of internationalization. Here again, we have to look at SMEs and firms characterization a move from step two to step three requires large capital resources and a completely different set of management styles. For example, at step two the most important quality a manager needs is good international sales quality, but at step three, not only is the manager required to have good sales quality, but also is require to have complete set of management skills consisting of control, motivation and training of foreign sales subsidiaries. In addition the managers should have an understanding of knowledge transfer between the sales subsidiary and the holding company and as well as skills that may be difficult to obtain in SMEs.

The finding from the study showed that one important criteria in the commitment decision-making of the firms to go from one step to the next is the risks reduction (fig. 6:3.5). As the establishment of the foreign sales subsidiary and/or local manufacturer and production require a large amount of financial and human capital, which will make the exit strategy costly. Companies should take special caution in their calculation of the host country’s risks before considering the investment opportunity.
What do you think is the most important criterion (Economic, Socio-cultural or Political) for Swedish investors on an investment (FDI) in new market (Iran)?

However, the country's risks play even more significant roles during the export mode step as many respondents in this study did bring up the difficulty in getting L/Cs in trade set-ups with Iran as the result of UN's sanctions. Those sanctions have increased the country's risks in the calculation of all international financial centres and that caused many of the firm’s loss of trade with Iran, even though their product was not the subject of the sanctions, simply because the companies were not willing to take this risk. (Fig: 6:3.6)

The negative impact of UN sanctions on Iranian SMEs has been devastating due to their limited resources. It has been more difficult for them to restructure their manufacturing or importing/exporting activities to adjust to the new situation and in many cases, they have been forced to obtain raw materials on the black market. Consequently, their profit margins have diminished and for many SMEs who just have domestic focus, high inflation has amplified this negative impact.

Even though there have been some minor indications regarding the development of the non-state sector and ceding on state-owned enterprise, as the result of lack of transparency in government’s agency, many people are quite suspicious about the
privatization process. Only one person believed that as a result of the government’s 4th Five Years Development Plan, there has been some improvement in the economy and SMEs environment in Iran. However, most respondents believed due to lack of sufficient implementation and planning, the transition period in Iran will be long and probably not effective. (Fig 6:3.7)

Figure: 6.3:7: the impact of globalization policy on trade

<table>
<thead>
<tr>
<th>Had privatization and trade liberation policy in Iran referring to government 4th Five years development plan, any impact on changes toward market economy and improvement in business environment in Iran?</th>
</tr>
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<td>No impact</td>
</tr>
<tr>
<td>Positive impact, the business environment has become better</td>
</tr>
<tr>
<td>Negative impact, the business environment has become worse</td>
</tr>
<tr>
<td>Do not know</td>
</tr>
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</table>

Referring to the data from Doingbusiness.org (appendix 3), Iran has moved from being ranked 131 in 2007 to 135 in 2008 (of 178 countries), in the overall “Ease of Doing Business.” This indicates that it has become overall much more difficult to do business in Iran, due to the additional procedures in place for starting a business and dealing with licenses and other government administrative work.

6.4 Summary of the Responses and Finding

The macro-environment elements --- political, economic, social, and technological forces --- have played a dominant role in the current Iranian business atmosphere. Even though not all those forces have a threatening impact on the business, the political and economic forces are the most influential and are the ones that have turned Iran into one of the riskiest countries in the world for the investor. The high market risks have strongly affected marketing and trading decisions in most firms. Poorly implemented and complex market regulations have devastated both domestic and foreign firms. The recent globalization policies and market deregulation and move toward privatization has been very slow and created a market flux. In addition to the laws, trades are also overseen by social codes and rules of religion ethics. Even the international and foreign policies that have caused the UN’s sanctions have added to this chaotic situation, and have made it so that no international financial institutions are willing to work with Iran. As a result of the UN’s sanctions and the high country risks, international trade with Iran has been interrupted and many firms have lost business.
Chapter 7 Conclusions

7.1 The Research Purposes

To answer the first question, regarding the impacts of the Iranian’s globalization policy on SMEs environment, the data shows a general deterioration of SMEs environment. However, it has been difficult to determine if this has been caused by government globalization policy or other factors as I did not have any control of other macro-environmental variables to isolate their impacts. But looking back at the barriers to the SMEs development (appendix: 5), the government subsidization of state-owned companies still exists, but I could not find data that showed the amount of the government subsidy to compare if there has been a reduction between the year 2005-2008. For example, examining the other barriers, such as the time-consuming registration procedures, the data shows that it has become even more difficult in 2008 than even in 2007 and it requires a longer time than it did previously. It was almost the same situation looking into the others barriers to SMEs development and it has been difficult to see any positive impacts of the government policies to overcome the barriers. However, as I could not find detailed information about Iranian SMEs performance in the last three years, it is tricky to come to a generalized conclusion. Even though there has been some indication regarding trade liberation, privatization and the change of economic structure and business environment in Iran, the evidence has not been strong enough to support my hypothesis, which said that that the change of government policy and regulations has affected the business environment toward market economy that has created new business buyer behaviour, which caused the trade reduction.

Regarding the 2nd question, which asked how the adaptation of new government policies has affected the international trade with Iran? All the evidence and data indicated that there is an enormous distraction in international trade, even though some countries have increased their export to Iran. Many of those exporters have faced more complexity as some had to change their bank or even change the distribution route, causing a delay in the shipment and thereby increasing the cost. However, the distraction was more likely as result of the impacts of the UN’s sanctions than the government’s trade policy.

Finally, regarding the last research question about the barriers and the reason behind Swedish trade reduction in Iran, the data indicated that the high country risk has been the main reason behind the trade reduction, though other reasons like high inflation and new competition had some influence in the reduction. The main barrier for the Swedish companies has been the lack of banking relations between the two countries to a degree
due to the UN’s sanctions. This is actually mainly due to a lightly-regulated banking system in Iran that limits any foreign bank’s activity in Iran and discourages the lack of joint ventures in the banking industry.

7.2 Remarks & Prospects for Further Studies

Unfortunately, due to the complexity in isolating all other independent macro-environmental variables impacts on the SMEs, it has been somewhat impossible to measure only the impacts of globalization and trade liberation polices on the SMEs environment. As the objectives of those polices were to overcome the barriers to SMEs development, I chose to examine barriers to SMEs to clarify if there have been any differences in that area or not. The data shows that most of those barriers still exist and there has not been much improvement in the last three years. In some cases, it has even become more difficult. It was complicated to determine if the failure was due to the policy or the shortfall in the implementation of the policy. Since there was more data supporting the shortfall of government implementation of its policies, it is important to further investigate the government’s execution process to elucidate obstacles. This is because it is more important to do things right than to do the right things. After accession of the WTO, Iran has tremendous opportunities for exporting their products in the international market. However the data from study indicate that not many of Iranian industries have enough surplus produce due to lack of efficient production facilities, weak management capacities, low labour productivity, low level of technology and inefficient communication and education. The international market access for Iran is commercially meaningless unless Iran strengthen its capacity to benefit from international trade by increasing its competitiveness through investment in development of human resources, enhancement of technological capability, strengthening of institutional capacity and supporting local SMEs, including linkages between SMEs and LSEs.

Even the government’s policy to entice foreign investors to direct investments in Iran has been fruitless. As this study only scratched the surface of the subject FDI in Iran, it requires deeper investigation into the motivation of foreign investors. This is because most often the motives of FDI are to achieve a competitively priced labour force, to have access to critical resources (Deeds and Hill, 1998)\textsuperscript{104} and to develop new knowledge and capabilities that enhance its international competitiveness (Shan and

As the data in Appendix 3, figure 8.7 shows, Iran has a much lower level of labour productivity than other developing countries. Therefore, it probably requires more intensive investment into education and labour training programs from the government to increase labour productivity and maintain the country’s competitive advantage. It would not be possible to attract investments without government providing the necessary support to SMEs.

The data has shown that the country high risk has been the main barriers to international trade. The high risks were caused by various internal and external sub-factors and barriers. Currently, the UN’s sanctions played a significant in the calculation of the country’s risk in the case of Iran. It still needs to be stated that there are other internal factors that were included in the focus of this study that were influential as well. For example, a lack of access to information was one important barrier in Iran, which played a different role in the company’s decision-making process. First, the country risk (CR) is equal to perceived risk (PR) and not to the actual risk (AR).

\[
CR = PR \quad PR > AR \quad \text{(if there is lacks of access to information)}
\]

\[
PR = AR \quad \text{(in the case of perfect information)}
\]

So a lack of access to information in Iran had actually increased the risks and made it more difficult for the international financial center to issue import/export credit, which interrupted much of the international trade with Iran. This lack of access to information in Iran affects even the company’s market commitment as Johanson & Vahlne, 1977 highlighted the positive correlation between market commitment and market knowledge. As the market knowledge and information play a significant role, both for international trade and FDI, it would be of interest to closely study its impacts on the management behavior and how Iran can overcome this barrier. For the improvement of the government policies, if we look at the country as a brand and at investors as its customer, understanding what is in the investor black box can help the government to manipulate the stimuli to get the desired outcome. For example it is of extreme necessity for Iran to re-examine the trends in information and communication technology development and develop ways by which Iran’s advantages can be maximized. One major advantage of promoting e-commerce in Iran is that it can provide relatively cheap access to global markets even for SMEs in remote areas.

As data from study indicated, some EC countries, and even some Swedish companies, had actually increased their export to Iran during the same period. It would be of interest to study the management behavior and the various ways the managers deal with the risks, as it showed that not all the managers did see high risk as a threat. Some even looked at it as an opportunity and mentioned that the high risk has stopped the competition in the Iranian market.
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http://www.haier.com/
http://www.lg.net

Iranian Government Globalization Policy Impacts on SMEs and the Corresponding Effect on Iranian-Swedish Trade
53(63)
Appendix: 1

Factors affecting on trade and industry in Iran

Factor 1:

Economic environment:
4th Five Year Development Plan (2005-2009) and Iranian Globalization policy from 2006

1. Higher import tax on finished goods
2. Lower income tax and tax reduction in the free trading area
3. Privatization and trade liberation
4. Higher trade support for SMEs
   a. Better information available
   b. Improvement of IT infrastructure
   c. Improvement of transportation and distribution
   d. Increase transparency in government economy policy
   e. Improvement of banking system and financial system

Factor 2:

Socio-cultural environment:

Most and less unchanged during the recent years

Factor 3:

Political environment:

1. International turbulence referring to Iranian nuclear activity and support of terrorist group in region and Iraq (western suspicion however Iran deny)
2. UN’s sanctions
3. Government change in 2005 to a more fundamental and hard-line regime

Some questions used during interviews:

1) How has your company’s trade with Iran been affected for the last 2 years?
2) Has the recent Iranian higher import tax on finished goods any impact on your trade?
3) What is the main export mode that your company use currently in trade with Iran?
4) How do you think the future of your company’s trade with Iran would be in the next 5 years?
5) How do you think the future of Swedish trade with Iran would be in the next 5 years?
6) What has been the affect of Iranian lower income tax and tax reduction in the free trading area on your company’s decision about investment in Iran?
7) Had privatization and trade liberation policy in Iran referring to government 4th Five years development plan, any impact on changes toward market economy and improvement in business environment in Iran?
8) What has been the impact of the recent political turbulence (Iranian foreign and nuclear policy, and UN sanction) on the trades and/or businesses in Iran?
9) What do you think is the most important criterion (Economic, Socio-cultural or Political) for Swedish investors on an investment (FDI) in new market (Iran)?
10) From your experience and in your opinion, what were/are the major problems and barriers Swedish companies had/have in the trade with Iran?
11) What do you think is the reason that Swedish-Iranian trade relations have become weaker in the recent years?
12) In your opinion, what impact has the Iranian privatization, trade liberation, globalization policy and in general recent events had on SMEs?
Appendix: 2

Figure 8.1

**Explore Economies**
This page shows summary Doing Business 2008 data for the selected economy. The first table lists the overall “Ease of Doing Business” rank (out of 175 economies) and the rankings by each topic. The rest of the tables summarize the key indicators for each topic and benchmark against regional and high-income economy (OECD) averages.

**Iran**
Region: Middle East & North Africa
Income category: Lower middle income
GNI per capita (USD): 5,999

<table>
<thead>
<tr>
<th>Ease of...</th>
<th>Doing Business 2008 rank</th>
<th>Doing Business 2007 rank</th>
<th>Change in rank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Starting a Business</td>
<td>135</td>
<td>131</td>
<td>-4</td>
</tr>
<tr>
<td>Dealing with Licenses</td>
<td>164</td>
<td>158</td>
<td>-6</td>
</tr>
<tr>
<td>Protecting Investors</td>
<td>158</td>
<td>158</td>
<td>0</td>
</tr>
<tr>
<td>Reforming the Insolvency System</td>
<td>141</td>
<td>143</td>
<td>+2</td>
</tr>
<tr>
<td>Registering Property</td>
<td>143</td>
<td>143</td>
<td>-2</td>
</tr>
<tr>
<td>Getting Credit</td>
<td>68</td>
<td>62</td>
<td>-6</td>
</tr>
<tr>
<td>Paying Taxes</td>
<td>135</td>
<td>129</td>
<td>-6</td>
</tr>
<tr>
<td>Trading Across Borders</td>
<td>57</td>
<td>54</td>
<td>-3</td>
</tr>
<tr>
<td>Enforcing Contracts</td>
<td>118</td>
<td>110</td>
<td>-8</td>
</tr>
</tbody>
</table>

Note: Doing Business 2007 rankings have been recalculated to reflect changes to the methodology and the addition of three new countries.

**Starting a Business**
The challenges of launching a business are shown below. Included are: the number of steps entrepreneurs can expect to go through to launch, the time it takes on average, and the cost and minimum capital required as a percentage of gross national income (GNI) per capita.

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Iran</th>
<th>Region</th>
<th>OECD</th>
</tr>
</thead>
<tbody>
<tr>
<td>Procedures (number)</td>
<td>8</td>
<td>9.7</td>
<td>5.0</td>
</tr>
<tr>
<td>Duration (days)</td>
<td>47</td>
<td>39.5</td>
<td>14.9</td>
</tr>
<tr>
<td>Cost (% GNI per capita)</td>
<td>53</td>
<td>50.9</td>
<td>51.1</td>
</tr>
<tr>
<td>Paid in Min. Capital (% of GNI per capita)</td>
<td>1.3</td>
<td>407.7</td>
<td>32.5</td>
</tr>
</tbody>
</table>

**Dealing with Licenses**
Shown below are the procedures, time, and costs to build a warehouse, including obtaining necessary licenses and permits, completing required notifications and inspections, and obtaining utility connections.

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Iran</th>
<th>Region</th>
<th>OECD</th>
</tr>
</thead>
<tbody>
<tr>
<td>Procedures (number)</td>
<td>19</td>
<td>19.4</td>
<td>14.0</td>
</tr>
<tr>
<td>Duration (days)</td>
<td>670</td>
<td>201.4</td>
<td>153.3</td>
</tr>
<tr>
<td>Cost (% of income per capita)</td>
<td>553.4</td>
<td>445.7</td>
<td>62.2</td>
</tr>
</tbody>
</table>

**Employing Workers**
The difficulties that employers face in hiring and firing workers are shown below. Each index assigns values between 0 and 100, with higher values representing more rigid regulations. The Rigidity of Employment Index is an average of the three indices.

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Iran</th>
<th>Region</th>
<th>OECD</th>
</tr>
</thead>
<tbody>
<tr>
<td>Difficulty of Hiring Index</td>
<td>11</td>
<td>25.8</td>
<td>25.2</td>
</tr>
<tr>
<td>Rigidity of Hiring Index</td>
<td>50</td>
<td>42.4</td>
<td>39.2</td>
</tr>
<tr>
<td>Difficulty of Firing Index</td>
<td>50</td>
<td>31.2</td>
<td>27.9</td>
</tr>
<tr>
<td>Rigidity of Employment Index</td>
<td>40</td>
<td>22.1</td>
<td>20.8</td>
</tr>
<tr>
<td>Nonwage labor cost (% of salary)</td>
<td>23</td>
<td>14.9</td>
<td>20.7</td>
</tr>
<tr>
<td>Firing costs (weeks of wages)</td>
<td>51</td>
<td>35.6</td>
<td>25.7</td>
</tr>
</tbody>
</table>

Source: [http://www.doingbusiness.org/ExploreEconomies/?economyid=91](http://www.doingbusiness.org/ExploreEconomies/?economyid=91)
Appendix: 3

Statistical overview of SMEs in Iran

Figure 8.2

Number and percentage of industrial firms and their employees by size category

<table>
<thead>
<tr>
<th>Category</th>
<th>1-5 employees</th>
<th>6-9 employees</th>
<th>10-49 employees</th>
<th>50-99 employees</th>
<th>&gt; 100 employees</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of firms</td>
<td>16,753*</td>
<td>12,418</td>
<td>22,318</td>
<td>2,022</td>
<td>1,584</td>
</tr>
<tr>
<td>Percentage</td>
<td>30.4%</td>
<td>22.5%</td>
<td>40.5%</td>
<td>3.7%</td>
<td>2.9%</td>
</tr>
<tr>
<td>Number of employees</td>
<td>62,778</td>
<td>89,572</td>
<td>423,630</td>
<td>133,315</td>
<td>588,944</td>
</tr>
<tr>
<td>Percentage</td>
<td>4.8%</td>
<td>6.9%</td>
<td>32.6%</td>
<td>10.3%</td>
<td>45.4%</td>
</tr>
</tbody>
</table>

Source: Statistical Yearbook of Iran 1375 (1996/1997)
Note: * The data in this column refer only to manufacturing firms and exclude artisanal enterprises.

Figure 8.3

Characteristics of industrial SMEs by size category

<table>
<thead>
<tr>
<th>Business category</th>
<th>% Share of value added</th>
<th>Productivity</th>
<th>Businesses %</th>
<th>Businesses Number</th>
<th>Employees %</th>
<th>Employees Number</th>
</tr>
</thead>
<tbody>
<tr>
<td>Small firms (1-5 employees)</td>
<td>17.3</td>
<td>24.5</td>
<td>91.6</td>
<td>334,630</td>
<td>41.8</td>
<td>752,204</td>
</tr>
<tr>
<td>Small firms (6-9 employees)</td>
<td>5</td>
<td>41</td>
<td>4.8</td>
<td>17,406</td>
<td>7.3</td>
<td>123,171</td>
</tr>
<tr>
<td>Small firms (10-49 employees)</td>
<td>11.7</td>
<td>57</td>
<td>3</td>
<td>10,985</td>
<td>12</td>
<td>201,727</td>
</tr>
<tr>
<td>Medium and large firms (&lt;50 employees)</td>
<td>66</td>
<td>100</td>
<td>0.6</td>
<td>2,263</td>
<td>38.9</td>
<td>651,342</td>
</tr>
<tr>
<td>Total</td>
<td>100</td>
<td>59</td>
<td>100</td>
<td>365,261</td>
<td>100</td>
<td>1,678,484</td>
</tr>
</tbody>
</table>

Note: The level of productivity of manpower is indexed against the productivity of firms having more than 50 employees (100).

Figure 8.4

Establishments engaged in trade and repair services by urban/rural areas, 1373 (1994/1995)

<table>
<thead>
<tr>
<th>Category</th>
<th>Retail sales and repair services of personal and household goods</th>
<th>Wholesale and Commission trade</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rural</td>
<td>Urban</td>
</tr>
<tr>
<td>Total country, all sub-sectors</td>
<td>194,541</td>
<td>723,702</td>
</tr>
</tbody>
</table>

Source: Small Industries Organization
Figure 8.5

**Principal Constraints faced by Iranian SME Exporters**

<table>
<thead>
<tr>
<th>Constraint</th>
<th>Impact of Constraint (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lack of access to factor of production and raw material markets</td>
<td>12.78</td>
</tr>
<tr>
<td>Old machinery and equipment</td>
<td>9.40</td>
</tr>
<tr>
<td>Lack of foreign marketing support</td>
<td>7.90</td>
</tr>
<tr>
<td>Lack of financial markets</td>
<td>19.82</td>
</tr>
<tr>
<td>Instability of economic and administrative laws</td>
<td>26.69</td>
</tr>
<tr>
<td>Other factors such as overall economic performance, exchange rate instability, and closed foreign policies</td>
<td>23.31</td>
</tr>
<tr>
<td><strong>Sum of all constraints</strong></td>
<td><strong>100.00</strong></td>
</tr>
</tbody>
</table>

Source: UNIDO, 2003

Figure 8.6

**Oil and non-oil exports, 1370-1378 (1991/921999/00) (Rials bn)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Exports</th>
<th>Oil Exports</th>
<th>Non-oil Exports</th>
<th>Ratio of Non-oil Exports to Total Exports</th>
<th>Ratio of Oil Exports to Total Exports</th>
</tr>
</thead>
<tbody>
<tr>
<td>1370 (1991/92)</td>
<td>2,204</td>
<td>2,026</td>
<td>178</td>
<td>8.79</td>
<td>91.21</td>
</tr>
<tr>
<td>1374 (1995/96)</td>
<td>25,320</td>
<td>19,631</td>
<td>5,689</td>
<td>28.98</td>
<td>71.02</td>
</tr>
<tr>
<td>1375 (1996/97)</td>
<td>29,373</td>
<td>23,938</td>
<td>5,435</td>
<td>22.70</td>
<td>77.30</td>
</tr>
<tr>
<td>1376 (1997/98)</td>
<td>29,400</td>
<td>24,354</td>
<td>5,047</td>
<td>20.72</td>
<td>79.28</td>
</tr>
<tr>
<td>1377 (1998/99)</td>
<td>30,181</td>
<td>24,893</td>
<td>5,288</td>
<td>21.24</td>
<td>78.76</td>
</tr>
<tr>
<td>1378 (1999/00)</td>
<td>28,102</td>
<td>22,202</td>
<td>5,000</td>
<td>20.57</td>
<td>73.43</td>
</tr>
</tbody>
</table>

Source: Export Promotion Centre of Iran

Figure 8.7

**Five-year trend of Labour Productivity Index (LPI) in Iran**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Rials per Worker</td>
<td>1,000</td>
<td>1,115</td>
<td>1,125</td>
<td>1,154</td>
<td>1,155</td>
</tr>
</tbody>
</table>


**Ten-year changes in Labour Productivity Index (LPI) in selected Asian countries, 1986-1995**

<table>
<thead>
<tr>
<th>Country</th>
<th>Iran</th>
<th>China</th>
<th>India</th>
<th>Malaysia</th>
<th>Republic of Korea</th>
<th>Pakistan</th>
<th>Japan</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ratio of 1986:1988 LPI</td>
<td>106.49</td>
<td>156.79</td>
<td>144.59</td>
<td>142</td>
<td>183.81</td>
<td>177.84</td>
<td>131.19</td>
</tr>
</tbody>
</table>

Source: Asian Productivity Organization
### Importing Countries of Non-oil Products from Iran

<table>
<thead>
<tr>
<th>Nr.</th>
<th>Market</th>
<th>Metric tons</th>
<th>Export in 1000 US$</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>United Arab Emirates</td>
<td>1,864,552</td>
<td>444,362</td>
</tr>
<tr>
<td>2</td>
<td>Germany</td>
<td>102,699</td>
<td>354,332</td>
</tr>
<tr>
<td>3</td>
<td>Azerbaijan</td>
<td>895,761</td>
<td>248,848</td>
</tr>
<tr>
<td>4</td>
<td>Italy</td>
<td>200,913</td>
<td>191,443</td>
</tr>
<tr>
<td>5</td>
<td>China</td>
<td>1,272,900</td>
<td>189,976</td>
</tr>
<tr>
<td>6</td>
<td>Turkey</td>
<td>382,139</td>
<td>165,529</td>
</tr>
<tr>
<td>7</td>
<td>India</td>
<td>1,015,974</td>
<td>152,524</td>
</tr>
<tr>
<td>8</td>
<td>Japan</td>
<td>472,373</td>
<td>126,728</td>
</tr>
<tr>
<td>9</td>
<td>Iraq</td>
<td>252,433</td>
<td>101,562</td>
</tr>
<tr>
<td>10</td>
<td>Ukraine</td>
<td>451,846</td>
<td>96,114</td>
</tr>
<tr>
<td>11</td>
<td>USA</td>
<td>4,781</td>
<td>98,693</td>
</tr>
<tr>
<td>12</td>
<td>Saudi Arabia</td>
<td>357,812</td>
<td>88,263</td>
</tr>
<tr>
<td>13</td>
<td>Turkmenistan</td>
<td>230,442</td>
<td>87,217</td>
</tr>
<tr>
<td>14</td>
<td>Uzbekistan</td>
<td>122,594</td>
<td>81,418</td>
</tr>
<tr>
<td>15</td>
<td>Kuwait</td>
<td>1,818,739</td>
<td>74,306</td>
</tr>
<tr>
<td>16</td>
<td>Korea Rep</td>
<td>524,398</td>
<td>73,515</td>
</tr>
<tr>
<td>17</td>
<td>Russian Federation</td>
<td>118,352</td>
<td>68,495</td>
</tr>
<tr>
<td>18</td>
<td>Pakistan</td>
<td>195,545</td>
<td>64,586</td>
</tr>
<tr>
<td>19</td>
<td>Thailand</td>
<td>360,462</td>
<td>53,417</td>
</tr>
<tr>
<td>20</td>
<td>Spain</td>
<td>92,211</td>
<td>52,741</td>
</tr>
<tr>
<td>21</td>
<td>Taiwan</td>
<td>282,634</td>
<td>52,423</td>
</tr>
<tr>
<td>22</td>
<td>Armenia</td>
<td>126,819</td>
<td>50,148</td>
</tr>
<tr>
<td>23</td>
<td>Hong Kong</td>
<td>38,622</td>
<td>49,249</td>
</tr>
<tr>
<td>24</td>
<td>France</td>
<td>25,632</td>
<td>44,761</td>
</tr>
<tr>
<td>25</td>
<td>Belgium</td>
<td>130,797</td>
<td>44,501</td>
</tr>
<tr>
<td>26</td>
<td>Singapore</td>
<td>300,964</td>
<td>43,127</td>
</tr>
<tr>
<td>27</td>
<td>Afghanistan</td>
<td>149,328</td>
<td>41,168</td>
</tr>
<tr>
<td>28</td>
<td>Switzerland</td>
<td>1,874</td>
<td>38,702</td>
</tr>
<tr>
<td>29</td>
<td>Syria</td>
<td>23,040</td>
<td>38,524</td>
</tr>
<tr>
<td>30</td>
<td>Rest of America</td>
<td>37,887</td>
<td>56,630</td>
</tr>
<tr>
<td>31</td>
<td>Rest of Europe</td>
<td>662,817</td>
<td>176,757</td>
</tr>
<tr>
<td>32</td>
<td>Rest of Asia</td>
<td>1,425,827</td>
<td>234,198</td>
</tr>
<tr>
<td>33</td>
<td>Rest of Africa</td>
<td>517,856</td>
<td>75,392</td>
</tr>
<tr>
<td>34</td>
<td>Pacific</td>
<td>11,290</td>
<td>12,806</td>
</tr>
</tbody>
</table>

Total: 14,272,373 Metric tons, 3,757,465 Export in 1000 US$
Appendix: 4


General policy

- Improvement of transparency in public sector organizations
- Improvement of Internet facility and training
- Reduce administrative, financial and judiciary corruption
- Active participation in international forums
- Acceptance of international copyright law
- Providing facilities for new industrial SMEs, especially in isolated locations lacking raw materials and intermediate goods, with the objective of creating employment in underdeveloped areas
- Attracting domestic and foreign investments
- Adjusting policies for expanding the share of industrial SMEs in GDP, inter alia by promoting women entrepreneurship
- Supporting all forms of employment-generating activities, including self-employment, entrepreneurial activities and group business activities in rural areas

Economic policy

- Property and personal rights, to support financial security for investor
- Promotion of market economy and free competition (limiting the dominance of public sector based on Article 44 under Constitutional law)
- Special attention to the social justice and support for social security and job support organization (unemployment office and other organization)
- Correct usage of monetary, fiscal and trade policy in order to reduce economy disturbance to achieve sustainable economical growth
- Support domestic production for quality improvement based on international organization for standardization
- Pass law and implementation of it for the support of creative work in order to promote and support service industry
- Support for creative and innovative scientific research and study in order to flourishing economy
- Use of education, human capital and new technology to promote non-oil export
- Improvement of the banking system and promotion of electronic banking
- Developing domestic financial resources to increase investments by introducing savings incentives and promoting small investments
- Developing and promote joint and foreign direct investment in modern technology and science
• Collaboration and empowerment of foreign diplomacy in order to improve active presence of Iranian product in international market
• Improvement of common relations with the Gulf and other neighbouring states
• Active presence at WTO and collaboration with other developing countries
• Development of tourist industry
• Providing funds to the Bank of Industry and Mines for setting up credit lines for industrial SMEs
• Developing the cooperative sector and encouraging entrepreneurial activities in it by introducing effective and sound support systems
• Simplifying the regulatory framework for investments in the manufacturing sector

Political policy
• Political freedom and respect for human rights
• Improvement of government relations with Iranians abroad
• Empowerment of local governments
• Reconsideration of the government’s foreign policy goals and tools, considering current international disturbance, the change of foreign policy implementation and more effective use of convening power beside traditional diplomacy
• Support and empowerment of non-governmental organization (NGO)
Appendix: 5

Summary of the barriers to SME development in Iran referring to UNIDO

• Market barriers:
  - Existence of purchasing monopolies (monopsonies)
  - Stringent nature of contracts SMEs have to conclude with LSEs
  - Existence of monopolised markets in various sectors
  - Fluctuations in supply and demand, specifically in the food industry
  - Government subsidization of state-owned companies, resulting in unfair competition
  - Lack of marketing mechanisms and resulting inability to access national and international distribution channels
  - Smaller volume in raw material purchases, resulting in higher prices

• Financial barriers:
  - Lack of commercial and specialised banks that would lend money to SMEs, and similar loan criteria for all categories of firms
  - Smaller firms have great difficulties in offering collateral for loans
  - Mounting liquidity pressure on SMEs following the adoption of contractionary macro-economic policies by the government
  - Delays in receipt of income from sales, leading to inability of banks to secure loans and liquidity pressure on SMEs, which drives them towards more expensive unofficial markets
  - Absence of joint ventures and lack of government facilities for forging joint ventures
  - Weak business environment for SMEs

• Lack of access to various kinds of information, including:
  - Marketing information (on domestic and foreign markets, price structures, packaging requirements, etc)
  - Information on the financial and technological standing of SMEs to enable investors to select healthy businesses for their investment
  - Technical and scientific information
  - Information on raw material suppliers and buyers

• Government policies:
  - Inability to create an enabling environment for SMEs
  - Policies that are harmful to SMEs, e.g. subsidies for state-owned firms

SMEs often have to refer to various government agencies for a variety of reasons, but often lack the necessary workforce or bureaucratic skills to negotiate effectively with these organizations.

Although the overall rate of tax collection is not high in Iran, the unequal collection of tax places a burden on firms that report their revenue status transparently and eventually encourages large-scale tax evasion.

The administrative hurdles for the collection of duties and the lack of institutions to resolve possible disputes arising from arbitrary decisions.

- **Legal barriers**
  - Complicated registration for entering into the tender business
  - The requirement for any start-up company to have a Board of Directors
  - The requirement for start-up companies to have at least two partners
  - Time-consuming registration procedures requiring up to three months to register a business
  - Lack of specialized courts to deal with trade disputes
  - Obsolete trade laws
  - Absence of a meaningful codification system
  - Inappropriate legal position of shareholders/managers
  - Lack of consistent and comprehensive legal framework for SMEs
  - Lack of differentiation between SMEs and LSEs in tax laws
  - Rigid and inflexible labour laws