

The Challenges for Sri Lankan SMEs in Entering the Clothing Industry Export Market

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Abstract

Research on small and medium-sized enterprises (SMEs) within the apparel sector has extensively explored their roles and contributions. However, there remains a notable gap in the literature concerning the specific challenges faced by Sri Lankan apparel SMEs when entering export markets. This study seeks to address this gap by examining how these enterprises navigate and sustain themselves within the industry, with particular emphasis on the barriers to export entry, the interrelationships among these challenges, and the identification of the most critical obstacles. The research identified four key thematic challenges: limited financial capacity, trade regulations and barriers, insufficient internal capabilities, and inadequate marketing knowledge. A purposive sampling strategy was employed, and data were collected through qualitative interviews with eight participants actively engaged in the SME apparel industry in Sri Lanka's Western Province. Thematic analysis was used to interpret the data and uncover recurring patterns. Findings indicate that financial constraints represent the most significant impediment to international expansion. Trade and regulatory barriers also exert considerable influence. Internally, managerial knowledge gaps and worker absenteeism were highlighted as major limitations, while marketing knowledge appeared to be the least prioritized area among Sri Lankan apparel SMEs. Based on these insights, the study offers practical recommendations for both SMEs and policymakers, including the development of targeted marketing strategies and the creation of a more supportive ecosystem to facilitate SME growth and export readiness.

Keywords: SMEs, Export Market, Clothing Industry

1. Introduction

1.1 Background of the study

Small and medium-sized enterprises (SMEs) constitute the backbone of the global economy, accounting for approximately 90% of all businesses and nearly 50% of global employment. In developing countries, SMEs are responsible for creating seven out of every ten formal jobs. Officially recognized SMEs contribute up to 40% of GDP in these regions, and when informal enterprises are included, this figure increases significantly. Projections indicate that 600 million new jobs will be required by 2030 to accommodate the expanding global workforce.

In Sri Lanka, SMEs contribute over 52% of the national GDP. However, their participation in international trade remains limited. The World Trade Report (2016), based on data from 25,000 SMEs in developing countries, revealed

that manufacturing and service SMEs contribute only 8.5% to total export revenues, compared to 34% in developed economies (Lakshman, Kumarasinghe, & Weerasinghe, 2023). In 2022, Sri Lanka's total exports reached USD 14.8 billion, ranking it as the 89th largest exporter globally, with an increase of USD 2.24 billion since 2017 (OEC, 2024). The apparel sector, in particular, stands out as the country's second-largest export industry and a key driver of export growth (OEC, 2024).

Despite this, SMEs in Sri Lanka contribute only around 5% to total exports, a figure significantly lower than that of other Asian economies such as China, where SME export participation exceeds 40% (Lakshman et al., 2023). This disparity highlights Sri Lanka's underperformance in integrating SMEs into global trade, particularly when compared to other emerging economies in the region.

The limited involvement of SMEs in exports is attributed to a range of internal challenges, including limited motivation to export, inadequate technological capabilities, low risk tolerance, a shortage of skilled labor, financial constraints, and limited firm size and experience. Additionally, external barriers such as fluctuating market demand, regulatory complexities, global competition, environmental uncertainty, and restricted access to information and resources further hinder SME export participation (Lakshman et al., 2023).

1.2 Industry Overview

This study focuses on the apparel industry, which accounts for 39.74% of Sri Lanka's total export earnings and employs approximately 15% of the country's industrial workforce (Export Development Board [EDB], 2024). The SME sector was selected due to its central role in the national economy, comprising 75% of all enterprises and contributing 20% to total exports, 45% to employment, and 52% to GDP (Alles, 2023).

1.3 Research Problem

Sri Lankan SMEs are currently facing significant challenges and are widely regarded as among the least prepared for an uncertain future (Alles, 2023). One of the most pressing issues is limited access to finance. SMEs are often denied bank loans and must rely on internal resources or family funding for initial capital.

Recent fiscal policy changes have further exacerbated these difficulties. The corporate tax rate has increased to 30%, affecting SMEs with annual earnings below LKR 500 million, including those engaged in export activities (PWC, 2023). This tax burden reduces profitability and limits reinvestment capacity, thereby hindering efforts to expand production, innovate, improve product quality, and invest in marketing and branding (Dayarathna et al., 2018).

Given these constraints, it is essential to investigate the specific challenges faced by SMEs in the apparel sector as they attempt to enter and sustain operations in the export market.

1.4 Rationale

Existing literature has paid insufficient attention to the distinct factors influencing SME export entry, as opposed to post-entry performance. Haddoud, Onjewu, Nowinski, and Jones (2021) argue that international business research often fails to differentiate between the determinants of initial market entry and those affecting long-term survival. Furthermore, Kasema (2022) notes that most export-related studies focus on firms in developed economies, overlooking the unique challenges faced by SMEs in developing countries. These include market analysis, location selection, timing of entry, and resource limitations.

In the Sri Lankan context, SMEs in the apparel industry face several pressing challenges, including a shortage of skilled labor, resource constraints, regulatory barriers, and financial limitations. Maintaining a seamless production process is particularly difficult due to high employee turnover, as workers frequently leave in search of better-paying opportunities. These challenges are exacerbated by the country's current economic instability.

Addressing these gaps is essential to support the growth and sustainability of Sri Lankan SMEs in the global marketplace.

1.5 Research Aim

This study aims to examine the challenges faced by Sri Lankan SMEs in entering the export market, with a specific focus on the clothing industry.

1.6 Scope

This research is confined to SMEs operating within Sri Lanka's clothing industry. Data will be collected from a sample of 10 interviewees. While the findings will provide valuable insights into the apparel sector, they may not be generalizable to the broader SME landscape either within Sri Lanka or internationally.

1.7 Significance

This study offers valuable insights for policymakers seeking to design targeted support programs for SMEs and make informed investment decisions. For SME owners and managers, the findings will facilitate proactive planning, informed decision-making, and collaborative problem-solving to enhance export readiness.

Understanding the barriers faced by Sri Lankan apparel SMEs is crucial for improving competitiveness, fostering innovation, and diversifying the industry. By addressing these challenges, the study aims to increase SME participation in international trade, thereby contributing to economic growth and job creation.

Given the strategic importance of the apparel sector and the intensifying global competition, this research can help SMEs tap into underexplored markets and strengthen their position in the global value chain.

2. Methodology

2.1 Research Design

2.2 Research Approach

This study adopts an inductive research approach, which is well-suited for exploring complex, context-specific phenomena. By analyzing qualitative data collected through indepth interviews, the study seeks to identify recurring patterns and emergent themes that reflect the lived experiences of participants (Azungah, 2018). This approach allows for theory development grounded in empirical evidence rather than testing pre-existing hypotheses.

2.3 Research Method

A qualitative research method has been employed to explore the challenges faced by Sri Lankan SMEs in the clothing industry when entering the export market. This method facilitates a comprehensive understanding of participants' real-life experiences. Specifically, semi-structured interviews were chosen to allow for both consistency across interviews and the flexibility to probe deeper

into individual perspectives, thereby enriching the data collected.

2.4 Sample

The study involved a purposive sample of 10 participants, including SME owners, employers, and directors within the Sri Lankan clothing industry.

2.5 Data Collection Methods

The primary data collection technique for this study is semi-structured interviews, which are considered more effective than other interview formats for eliciting rich, detailed responses (Ruslin, Mashuri, Rasak, Alhabsyi, & Syam, 2022). This method provides a balance between structure and flexibility, enabling the researcher to explore key themes while allowing participants the freedom to express their views in depth. An interview guide comprising openended questions was used to facilitate discussion and encourage participants to share their personal experiences and insights.

2.5 Data Analysis

The data was analyzed using thematic analysis, a widely recognized method in qualitative research for identifying, analyzing, and interpreting patterns within textual data (Naeem, Ozuem, Howell, & Ranfagni, 2023). This systematic approach ensures that the findings are grounded in the data and provide meaningful interpretations of the challenges faced by SMEs.

3. Analysis and Findings

The analysis draws upon thematic patterns identified in the literature and reinforced through empirical evidence gathered during the interviews.

The sample was purposefully selected to include individuals actively engaged in the Sri Lankan apparel industry, ensuring relevance and depth in understanding the challenges faced by SMEs in this sector.

3.1 Lack of Financial Capabilities

Financial constraints emerged as a dominant theme across the interviews. As noted by Dubey and Das (2022), financial resources are a critical competitive advantage for SMEs, yet many lack the necessary capital to support business operations and international expansion. Participants consistently emphasized the importance of financial strength in areas such as procuring raw materials, upgrading machinery to meet export standards, and investing in innovation to access new markets.

Participant P2 remarked:

"If I plan for the April summer season, I should have the necessary raw materials ready by January. That's a big challenge - it's costly. We need to be ready to spend immediately, and we cannot afford delays. It's actually difficult."

Similarly, P7 highlighted:

"We face many financial issues, especially in acquiring machinery suitable for export-quality production. Our current equipment does not meet the required standards."

These observations align with Paplikar (2023), who underscores the role of financial resources in enabling access to strategic investments, product development, and market expansion. Participant P2 further elaborated:

"Seasonality is crucial for international market reach. We must offer fresh innovations and timeless fashion. To do this, we need adequate human capital, financial resources, and material availability."

The collective responses indicate that financial limitations are a significant barrier to internationalization for Sri Lankan clothing SMEs. Most participants expressed difficulties in securing funding for various operational needs.

SMEs often rely on personal or familial financial support due to limited access to formal credit channels. This was echoed by several participants who shared their experiences with Sri Lankan banks.

P8 explained:

"When I started this business, no one supported me. I presented my proposal to the bank, but they rejected it. They said I needed a minimum income of LKR 5 million to qualify for a loan. They don't support SMEs at the inception stage."

P4 added:

"I've obtained several loans, but the process is extremely time-consuming. Some approvals took up to one and a half years. Even small loans require extensive documentation and long waiting periods."

P3 described a similar experience:

"Due to financial issues, we collaborated with other companies to fulfill bulk orders. We've had some exposure to exports, but not directly. I approached banks and financial institutions, but the process is exhausting. The paperwork is extensive, and even after submission, it takes months to get basic information like interest rates. In some cases, we waited nearly a year for a decision. It's not a pleasant experience."

Interestingly, P1 offered a contrasting perspective:

"I'm a bit cautious about loans. We built the business through bootstrapping - reinvesting profits slowly over time."

P1's approach reflects a preference for self-financing and aligns with Gunatilake (2016), who found that a lack of understanding of banking procedures can hinder SME growth and expansion.

3.2 Trade Regulations and Barriers

The Sri Lankan apparel industry has faced considerable operational challenges due to recent changes in trade policy. According to the International Trade Administration (2022), the imposition of a 15% Value Added Tax (VAT) on imported textiles and a 5% VAT on imported fabrics has led to significant price increases. This policy shift has directly impacted the cost structure of SMEs operating in the sector. Six out of eight participants in this study reported substantial hikes in raw material costs as a result of the newly introduced VAT.

Participant P7 noted:

"VAT issues do not directly affect our company, but when we source raw materials locally, we observe price increases because those materials are subject to VAT."

Similarly, P5 stated:

"Raw material costs have risen dramatically. However, we are constrained to sell at current market prices. If we export, we must absorb the additional costs. VAT is causing financial strain across the industry."

Ranasinghe (2023) warns that rising taxes and electricity tariffs may lead to the closure of many small businesses in export-oriented sectors. Specifically, SMEs are at risk due to a 15% to 30% increase in export revenue tax and a 65% rise in electricity costs. These findings were corroborated during the participant recruitment phase, where the researcher observed that several clothing SMEs had already ceased operations due to escalating costs of materials and utilities.

Participant P6 shared:

"Raw materials are increasingly scarce. We face issues with colour matching and quantity. For instance, matching lace with the same colour thread has become difficult. There are also other challenges related to limited imported supplies in the domestic market."

P6's remarks highlight the difficulties in sourcing essential accessories for production. These challenges align with findings from Economy Next (2022), which reported that Sri Lankan apparel manufacturers face delays in raw material shipments due to currency shortages, import clearance delays, and port congestion.

The evidence presented suggests that trade regulations and logistical barriers significantly hinder Sri Lankan clothing SMEs' ability to access necessary inputs. A supportive regulatory environment is therefore essential to foster export growth and enhance local competitiveness. Such an environment should include streamlined procedures for international market entry, legislative stability, and the implementation of innovative, exportoriented programs tailored to SME needs.

Participant P2 expressed concerns regarding institutional support:

"There is a lack of support. For example, largescale businesses can easily find export buyers through the Export Development Board. But for small-scale businesses like ours, unless we have personal contacts, we must visit the Board, submit our profiles, and explain our products. While they do offer some assistance, the process is slow and cumbersome."

P2's experience reflects the findings of the Asian Development Bank (ADB, 2019), which identified institutional inefficiencies as a barrier to SME export readiness.

Logistics companies increasingly rely on advanced technologies and rapid adaptation. SMEs, however, often struggle to keep pace with these developments, particularly in establishing e-commerce platforms and negotiating competitive rates with third-party logistics providers.

Participant P1 elaborated:

"Shipping is a major challenge. Using local shippers or third-party services like DHL or Aramex is very expensive—about 20 to 25 dollars per 900 grams. We occasionally ship abroad to customers who have migrated, but the cost is high. Even third-party rates are steep, and we must account for documentation weight. The entire supply chain is costly and complex."

These insights collectively illustrate how trade regulations, institutional inefficiencies, and logistical constraints pose significant barriers to export participation for Sri Lankan clothing SMEs.

3.3 Lack of Internal Capabilities

Safari and Saleh (2020) argue that the organisational decision-making structure plays a pivotal role in SME internationalisation, with managerial and psychological constraints often emerging as significant barriers to entering foreign markets. Consistent with this view, several participants in this study, as well as the researcher's observations, identified a lack of market entry knowledge as a major obstacle for Sri Lankan apparel SMEs seeking to engage in export activities.

Participant P8 stated:

"It's the knowledge. People don't understand how to get started or where to begin. They lack basic knowledge and the initial steps. There are professionals for that. It's important to reach out and acquire fundamental knowledge first." This highlights the importance of understanding foundational procedures before initiating export operations. Similarly, Madushanka and Sachitra (2021) found that SME export entry and performance are significantly influenced by managerial mindset, including attitudes toward risk, market knowledge, commitment, and awareness of export challenges.

Participant P1 shared:

"We haven't pursued any foreign orders, to be honest. My objective is to build the brand." "I'm a marketer, but I tend to be risk-averse. Marketers usually take risks and move forward, but I'm cautious."

These responses suggest that leadership mindset and strategic priorities significantly influence export decisions. Participant P4 also noted that limited knowledge of export procedures affects SMEs' ability to enter international markets.

In addition to knowledge gaps, workforce-related challenges were frequently cited. Chandra et al. (2020) emphasize that an effective workforce is essential for maintaining competitiveness in export operations. However, developing countries often face difficulties in attracting, training, and retaining skilled labor. All participants in this study reported that absenteeism and high turnover rates among workers have severely disrupted daily operations.

Participant P3 explained:

"I work with a mostly semi-skilled local workforce. The machinery we use requires less technical expertise than in competitive markets. I try to manage production with proper timing and technique, but frequent absenteeism, mostly due to personal reasons, makes optimization difficult."

Chandra et al. (2020) further note that shortages in production, marketing, logistics, and compliance staff can directly impact the internal functioning of apparel firms.

P3 added:

"When skilled workers don't show up, it affects daily output. Over a month, this becomes a major issue in meeting delivery deadlines. No buyer wants to work with a supplier who consistently delays orders."

This illustrates how persistent absenteeism can reduce production efficiency and jeopardize client relationships. The Sri Lankan garment sector predominantly employs female workers, 70% of whom often become inactive due to factors such as marriage, maternity leave, and childcare responsibilities.

Participant P1 elaborated:

"Absenteeism is a problem in our factory. Most of our workers are women, so when their children fall ill or have exams, they miss work. It's definitely an issue in the blue-collar category. In contrast, our office staff, mostly young people, so they don't pose such problems. The office feels like a family, not in terms of relatives, but in terms of culture."

This underscores the gendered nature of workforce challenges in the apparel sector, particularly in production environments.

Moreover, Safari and Saleh (2020) argue that poor leadership skills exacerbate internal organisational issues, including inefficient management practices, weak decision-making capabilities, and internal corruption. In contrast, transparent and inclusive leadership can mitigate such challenges.

Participant P8 described their approach:

"We hold monthly team meetings to discuss any issues and provide solutions. We maintain transparency with the team. We don't hide problems; we address them together. When management and staff are aligned, issues don't escalate."

This aligns with Hofmann and Strobel (2020), who emphasize that internal transparency enhances employee satisfaction by facilitating access to information and encouraging feedback.

3.4 Lack of Marketing Knowledge

Abubakari et al. (2022) argue that successful export marketing outcomes for SMEs depend not only on marketing knowledge, but also on the ability to effectively apply that knowledge through relevant competencies. This was reflected in the responses of participants P1 and

P2, who emphasized the importance of cultural sensitivity in developing overseas marketing campaigns and tailoring products to resonate with international audiences.

Participant P1 noted:

"Creativity is key. For example, someone in Europe or the USA might not relate to a model who looks Sri Lankan or Indian. You may need to use the right person for the campaign."

This aligns with Abubakari et al. (2022), who highlight the importance of cultural considerations in selecting marketing visuals that appeal to target markets. Similarly, Madushanka and Sachitra (2021) found that successful local marketing campaigns can indirectly attract international orders, thereby facilitating export entry.

Participant P2 shared:

"I haven't specifically targeted overseas customers in my campaigns. I currently boost posts targeting a Sri Lankan audience. However, I still receive inquiries from abroad, from India, from the UK, because people are watching. But I haven't responded to those requests yet. When they ask for product catalogs, I can't proceed because we don't specialize in seasonal manufacturing for international markets."

This illustrates how even domestically focused marketing can generate international interest, though a lack of readiness and strategic planning may prevent SMEs from capitalizing on such opportunities.

Davcik et al. (2021) emphasize that marketing capacity is shaped by an organisation's strategic planning and the resources available to conduct market research and implement distribution strategies. Participant P3 reflected on the impact of resource constraints:

"I currently handle marketing myself. I have the experience and qualifications, and I've been doing it for the past three years. We had a dedicated marketing person, but due to COVID and the market downturn, we had to eliminate that position."

This supports Davcik et al.'s (2021) assertion that the absence of a structured marketing plan and adequate funding can hinder the

implementation of new services and the retention of skilled professionals. Only a few participants in this study had experience with marketing campaigns, and even fewer operated e-commerce platforms.

Madushanka and Sachitra (2021) also report that most Sri Lankan clothing SMEs struggle to develop e-commerce capabilities, despite the potential to reach broader local and international audiences.

4. Conclusion

This study identified several critical barriers hindering the internationalisation of Sri Lankan clothing SMEs. Among these, financial limitations emerged as the most significant, with participants consistently citing difficulties in securing adequate funding for essential export-related activities such as raw material procurement, hiring skilled professionals, investing in marketing, and upgrading machinery.

Marketing capabilities were the theme participants, emphasized among revealing a potential gap in marketing knowledge, experience, and strategic commitment. This deficiency may represent a substantial obstacle for SMEs attempting to navigate and compete in international markets.

The findings underscore the importance of addressing both structural and capability-based challenges to support the successful internationalisation of SMEs. This research contributes to a broader understanding of the export entry process and offers practical insights for policy development and SME support initiatives.

5. Recommendations

SME decision-makers should adopt robust financial management strategies to improve working capital management, capital structuring, and accounting systems. This will strengthen their financial resilience and readiness for export activities.

Digital platforms offer cost-effective avenues for reaching global audiences. As of early 2024, Sri Lanka had 12.34 million internet users (56.3% penetration) and 7.5 million social media users (34.2% of the population) (Kemp, 2024). With over five billion global social

media users expected to rise to six billion by 2028, SMEs should invest in consistent digital marketing campaigns across platforms like Facebook and Instagram. Organic content and paid partnerships can significantly expand brand visibility and customer reach.

Effective management is essential for organisational success and competitiveness. According to Orji, Emmanuel, and Egwuatu (2023), rare, valuable, inimitable, and nonsubstitutable (VRIN) resources—such as managerial skills—can provide SMEs with a sustainable competitive advantage. Training in digital marketing, employee development, and strategic planning can enhance SME performance and long-term viability.

Trade authorities should introduce supportive regulations and initiatives tailored to the needs of export-oriented SMEs. These may include financial assistance programs, simplified export procedures, and capacity-building workshops. Government-led training sessions on export readiness, digital marketing, and international compliance standards could empower SMEs to compete more effectively in global markets.

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