

Accelerating Small and Medium-Sized Enterprise (SME) Digitalisation in Malaysia

2022/2023





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Forewords



Mahadhir Aziz
CEO of MDEC

Malaysia Digital Economy Corporation (MDEC), as Malaysia's lead digital economy agency, welcomes the findings of PayPal's Accelerating SME Digitalisation in Malaysia report. This report provides valuable insight into the digital state of Malaysia's SMEs, the backbone of the nation's economy. By understanding where we stand, we can craft more meaningful and targeted catalytic programmes that will ensure no one is left behind.

This report also reflects the accelerated digitalisation of Malaysia's economy in the past two years, and an endorsement of the efforts of the Malaysian government and MDEC in preparing the nation towards digitalisation. This is a journey that began 26 years ago with MSC Malaysia, which laid the foundations of a digital ecosystem.

This digital bedrock has enabled us to understand the importance of driving digital adoption among SMEs and smaller businesses during the COVID-19 pandemic. It allowed us to ramp up efforts via initiatives under the Short-Term Economic Recovery Plan (PENJANA 2020) and various initiatives under Budget 2021 and 2022.

We wanted to ensure that SMEs in Malaysia can undergo multiple levels of digital adoption, and as such, have provided various digitalisation grants that include the SME Digitalisation Grant, the Smart Automation Grant, the 4IR Catalyst Grant and the Global Technology Grant.

As we transition into the next phase of COVID-19 and beyond, we intend to keep this massive momentum going. Our next digital journey is marked by the launch of Malaysia Digital, which seeks to encourage and attract companies, talents, and investments while enabling Malaysian businesses and the Rakyat (people) to play a leading part in the global digital revolution.

The initiative is the engine that accelerates the growth of our digital ecosystem within nine focus areas, which includes Digital Trade, which seeks to drive cross-border trade with a level playing field via eCommerce, while standardising data exchange for efficient payment and collection through a national eInvoicing component.

This report will prove invaluable in our digital economy journey, and I hope that it will empower you to take this journey with us.

Thank you, and happy reading.

Fabian Bigar

CEO of MyDigital

Introduced in 2021, the Malaysia Digital Economy Blueprint (MDEB) is a wide-ranging blueprint with multiple participants and collaborators, and even more potential beneficiaries cutting across every facet of society, economy, and government.

The digitalisation of micro, small and medium enterprises (MSME) has been outlined as one of the drivers of change that will drive national development. As such, efforts are being made to increase the resilience of the MSMEs through the adoption of digital technology and assisting the entrepreneurs who were severely affected by the pandemic and who have lost their income. This includes accelerating take-up of incentives, subsidies, or assistance programmes; and streamlining the understanding and communications on the various support measures available from the different Ministries and agencies.

In 2021, Malaysia exceeded the target of 875,000 MSMEs adopting e-commerce by 2025, which is four years ahead of schedule. Over 890,000 MSMEs have adopted e-commerce as of the end of last year and the target has now been revised to 1.1 million MSMEs by 2025.

PayPal's report Accelerating SME Digitalisation in Malaysia found that, in order to drive digitalisation among SMEs, it is imperative to leverage digital payments, enhance public-private collaboration, empower women entrepreneurs, train SMEs in cybersecurity and data protection, and increase awareness and reach of government digitalisation initiatives.

I would like to congratulate PayPal for successfully producing this report to guide policymakers and highlight opportunities for greater public-private collaboration to accelerate the digitalisation of SMEs in Malaysia.



Introduction

During the COVID-19 pandemic, the rapid acceleration to digital channels and e-commerce was a major challenge for SMEs. A March 2020 study by the Malaysian home services platform, *Recommend.my*, found that more than two-thirds (68.9%) of Malaysian SMEs had lost more than half their business within a week of the first movement control order (MCO) that was issued by the Malaysian authorities to curb the spread of the virus.¹ In an address to the nation in May that same year, then-Malaysian Prime Minister Tan Sri Muhyiddin Yassin estimated that the economy of Malaysia had lost an estimated RM2.4 billion (US\$ 573.48 million) daily over the first two months of the MCO.²

As the Malaysian e-commerce sector began to flourish, necessity drove increasing numbers of Malaysians online. Along with the rest of the world, Malaysian households began to shop for both daily essentials as well as other goods and services online. With the widespread adoption of remote working policies and practices, online shopping for groceries and the popularity of food delivery apps surged alongside demand for virtual workouts, hobby classes for adults, and virtual educational services for youth. According to an August 2021 report by Facebook Business (now Meta) and Bain & Company, the share of digital consumers in Malaysia grew by 5% from 2020 to 2021, reaching 88% of Malaysia's consumer population³ - the highest by percentage share in Southeast Asia.⁴

Given the continued growth of the e-commerce sector in Malaysia and the importance of the SME sector to the economy, the Malaysian government's Economic Planning Unit launched the Malaysian Digital Economy (MyDIGITAL) Blueprint in February 2021. This blueprint was timely as the third wave of the coronavirus had already begun devastating Malaysian businesses and the economy. It strongly emphasises the importance of digitalisation for the country's economic recovery and lays out key strategic directives and initiatives that would facilitate the digital transformation of the Malaysian economy. MyDIGITAL also recognises digitalisation as key to strengthening Malaysian small businesses' ability to scale and sell cross-border.

Over the last six decades, Malaysia has moved up the global economic value chain from a resource-dependent economy driven by commodities exports and agriculture to a vibrant and innovative regional hub that is marked by the sectoral diversity and dynamism of its firms and industries.⁵ SMEs are the backbone of the Malaysian economy. As of 2020, there were more than 1.15 million SMEs in Malaysia, constituting 97.2% of all business establishments in the country.⁶ These SMEs employ nearly half (48%) of all workers in Malaysia, providing 7.25 million jobs in 2020.⁷

The Malaysian SME sector is diverse, vibrant, and holds immense potential for international growth and expansion. In 2021, a majority (83.8%) of the SMEs in the country belonged to the service sector, followed by construction (8%); manufacturing (5.8%); and agriculture (1.9%).

Recognising the SME sector's importance to the economy, the Malaysian government has invested significantly in programmes and projects aimed at helping Malaysian enterprises to succeed. While digitalisation and investment in technology had always been recognised as important drivers of SME success, the onset of COVID-19 and consequent lockdowns across Malaysia placed digital transformation at the forefront of policy efforts to sustain and develop the Malaysian SME sector.

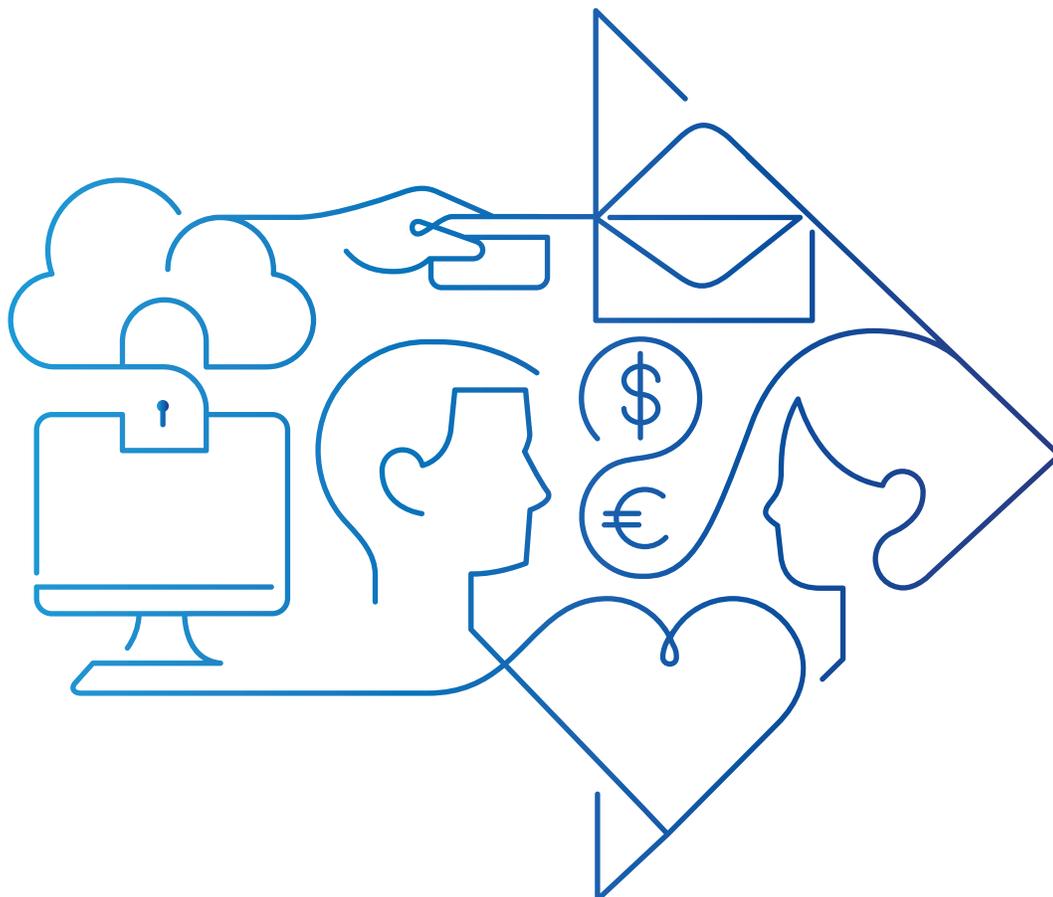
These efforts are especially crucial against the backdrop of a 2018 study by the World Bank that examined the

Malaysian digital economy and found that Malaysian businesses had lagged behind their international counterparts in digital adoption.⁸ According to the study, only 62% of all Malaysian businesses were connected to the internet, with an even lower share (46%) having access to a fixed broadband connection.⁹ The study also found that SMEs were especially underrepresented in the Malaysian digital economy as e-commerce adoption has been more prevalent amongst large export-oriented firms in the country.¹⁰

Hence, PayPal has conducted this study to examine the digital readiness of Malaysian SMEs and identify the drivers that could accelerate SME digitalisation. The goal of this report is to analyse and understand the progress that has been made in the digitalisation of these enterprises, the impact that digitalisation has had on their ability to sell cross-border, and to identify solutions to address challenges as well as to capture new opportunities. The report leverages PayPal's unique perspective as a digital payment provider that bridges Malaysian enterprises and their customers across the world, alongside the following primary and secondary sources:

- The 2022 PayPal Accelerating SME Digitalisation in Malaysia Survey, capturing responses from 1,000 SMEs¹¹
- Detailed long-form anonymised interviews with Malaysian SMEs
- In-depth review of existing literature

PayPal aims to provide a snapshot of Malaysia's SME ecosystem with respect to digitalisation during a time when the country and the rest of the world emerges from the pandemic, and to gain deeper insights into the Malaysian SME sector, its digital progress, and the potential for further growth.



Digital Adoption

In the post-pandemic world, digital transformation is no longer a nice-to-have, but a matter of survival especially for SMEs, not least because digitalisation enables SME to (i) carry out transactions even at a physical distance; (ii) to deliver goods efficiently with the use of AI-driven smart logistic solutions and digital delivery platforms; (iii) gain access to financial services, including SME credit; as well as (iv) to connect and engage with existing customers and to acquire new ones amid lockdowns and other restrictions.¹² Government lockdowns and movement control orders due to COVID-19 made digitalisation vital to the survival of small businesses in Malaysia. As early as June 2020, EY reported that 37% of SMEs in the country had taken steps to expand their technology capabilities at the start of the pandemic. In June 2021, according to the World Bank's COVID-19 Business Pulse Survey, 61% of small businesses and 62% of medium businesses had increased their use of digital platforms while 54% of small businesses and 81% of medium businesses had invested in digital solutions.¹³

In Malaysia, firms that have implemented some degree of digitalisation have produced tangible results. According to a joint study by Huawei and the University Consortium of Malaysia, SMEs using social media and e-commerce saw 26% to 27% higher productivity improvements while SMEs using data management solutions reported a 60% benefit impact on their productivity.¹⁴ Additionally, a 2020 study by Cisco estimates that digitally mature Malaysian SMEs could contribute an estimated additional RM99 billion (US\$23 billion) to the country's GDP by 2024.¹⁵

Despite commercial and economic opportunities, prior to the pandemic, Malaysian SMEs were slow to digitalise. The World Bank noted, "Malaysian businesses have adopted associated technologies less readily than the Malaysian government or population (relative to expectations based on per capita income). And Malaysia has less international internet bandwidth, fewer businesses with websites, and fewer secure servers than per capita income would predict — ranking far behind OECD countries in these measures despite being comparable on measures related to adoption by the government and people."¹⁶ Despite programs to encourage digitalisation, Malaysian SMEs lagged behind large firms in embracing digital transformation and thriving in the digital economy.

The relatively slow rate of technology adoption of Malaysian SMEs is surprising given the high levels of internet access (90%) in the country¹⁷ and that the majority of Malaysian consumers are also receptive to emerging technologies including Artificial Intelligence, facial recognition, and 5G.¹⁸ According to the Malaysian thinktank Khazanah Research Institute, this might be caused by factors such as employee skill sets, costs of digitalisation measures, and the need for additional consumer and data protection regulations.¹⁹ These issues have been rightly identified by the Malaysian government which has begun to place the digitalisation of SMEs at the heart of its economic recovery strategy. We hope that the results of our survey and analysis will further augment the government's efforts to accelerate SME digitalisation in Malaysia.

Survey Demographics

PayPal's survey was administered to a geographically diverse sample of 1,000 SME owners and decision makers.²⁰

In order to ensure that SMEs at various stages of digitalisation were represented in the survey, PayPal utilised non-probability quota sampling. This method ensured that the sample included online (n=400), offline (n=200), and hybrid [both online and offline] (n=400) SMEs from across all 13 states and three federal territories of Malaysia. Online SMEs are defined as those that sell their products and services through the internet; offline SMEs' sales and transactions are conducted through physical locations; and hybrid SMEs sell through both online and offline channels. For the purposes of this study, the definitions of online, offline, and hybrid depend entirely on the mode of sales. That is, an offline SME can still be considered to have digitalised if it uses technology for its operations such as inventory management software or digital payment tools. In other words, offline SMEs do not necessarily mean that they have no digital capabilities.

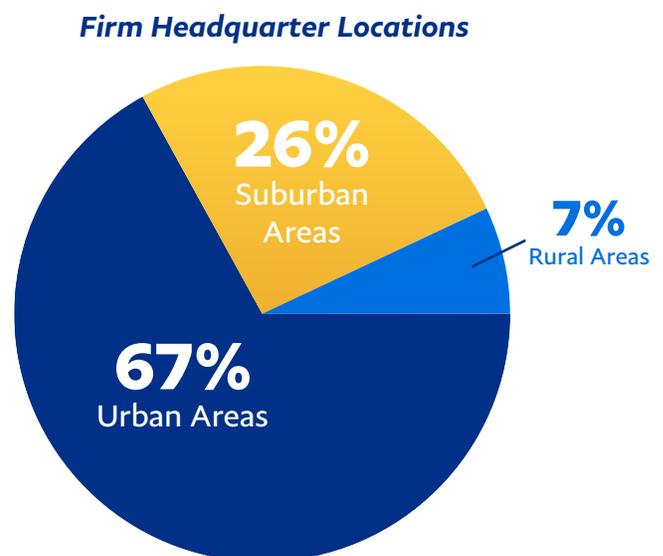
The survey provides an insightful snapshot of the entrepreneurial ecosystem in Malaysia. The SME sector in Malaysia is incredibly diverse and products and services offered by Malaysian SMEs range from food & beverages and fashion to healthcare and home improvement.

Malaysia's entrepreneurial ecosystem comprises both traditional enterprises and new players. More than a quarter (26%) of respondent firms have been in business for more than ten years while newer firms – two years or less – constitute 17% of the sample. Micro-enterprises (annual turnover less than RM 300,000) constituted 35% of the sample and larger SMEs with revenues between RM3 million and RM20 million constituted 24% of the sample. Additionally, SMEs with fewer than five employees made up slightly more than one-fifth of the sample (22%) while those employing 200 employees or more constituted a

similar share, at 20% of the sample.

The majority (67%) of respondent firms have their headquarters in urban areas, followed by 26% in suburban areas, and the remaining seven percent in rural areas (See Figure 1). This trend reflects Malaysia's population distribution as 77% of Malaysians live in cities.²¹

Figure 1



Additionally, the concentration of newer firms is relatively higher in rural areas – with 4 in 10 (41%) respondents from rural areas having been in business for two years or less, as compared with 13% of SMEs in urban areas and 18% of SMEs in sub-urban areas. In urban and suburban areas, established SMEs are more prevalent – with 69% of all urban and 63% of all suburban firms having been in business for five years or more. Moreover, 26% of urban and 30% of suburban small businesses have been operating for more than ten years.

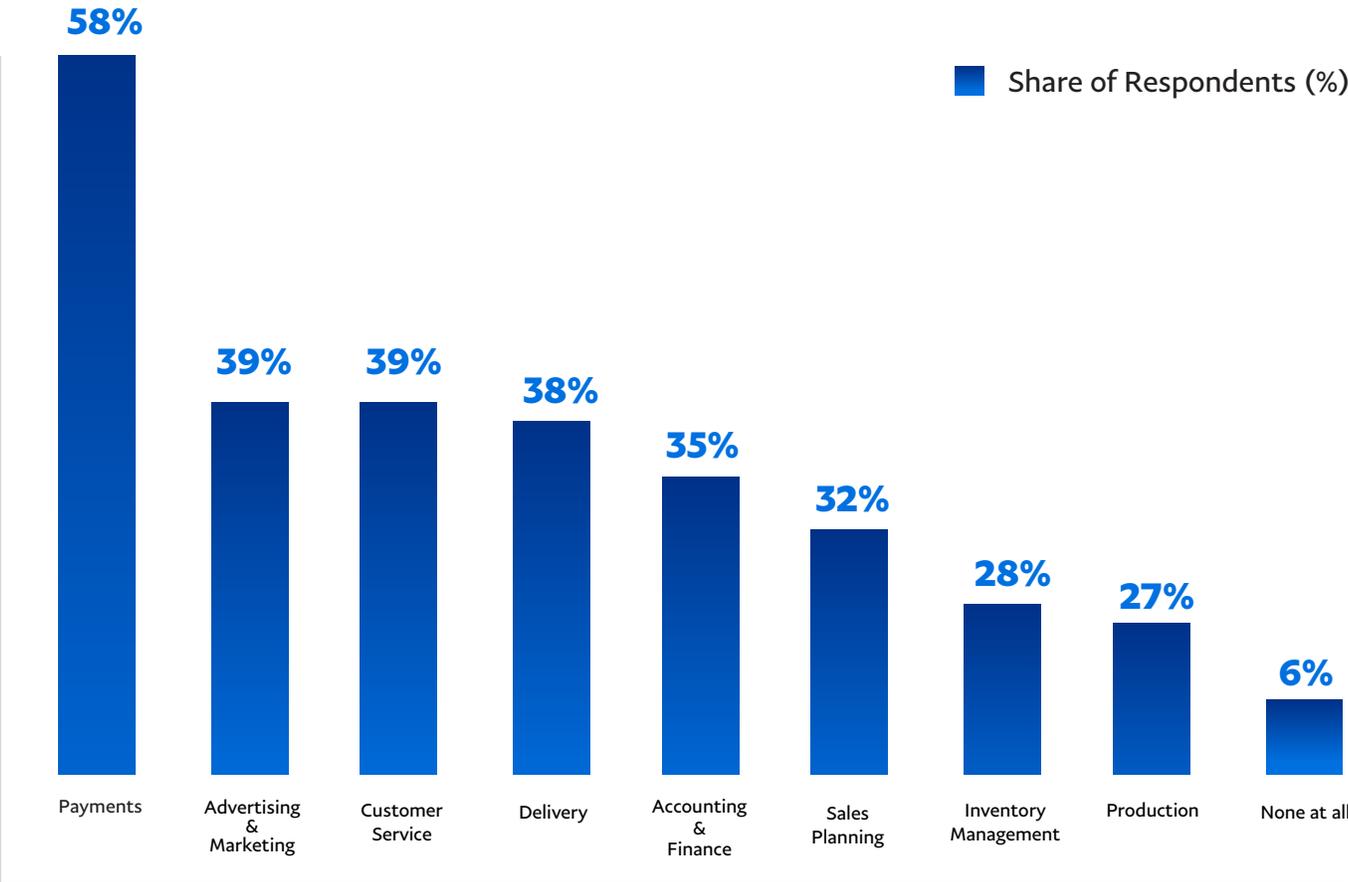
The State of SME Digitalisation

Digitalisation is a broad term and can include any integration of digital tools and technology into any aspects of a business. While many larger firms tend to adopt a holistic digital transformation strategy from the onset or to invest significantly in comprehensively digitalising their operations and processes, small businesses often have to make difficult decisions due to resource constraints and the need to identify critical business areas for digitalisation. For example, Malaysian SMEs tend to focus first on digital payments – nearly 6 in 10 (58%) of all the SMEs we surveyed had digitalised their ability to make and receive payments (See Figure 2). After payments, advertising and marketing as well as customer service are prioritised for digitalisation with 39% of SMEs having utilised digital tools in these areas.

Additionally, more than one-third of the SMEs (38%) had digitalised their delivery processes and a nearly equal share (35%) had digitalised accounting and financial needs. It is clear that the pandemic has shifted mindsets and accelerated SMEs digitalisation across many areas given that only six percent of businesses stated that they have no plans to digitalise their business.

Figure 2

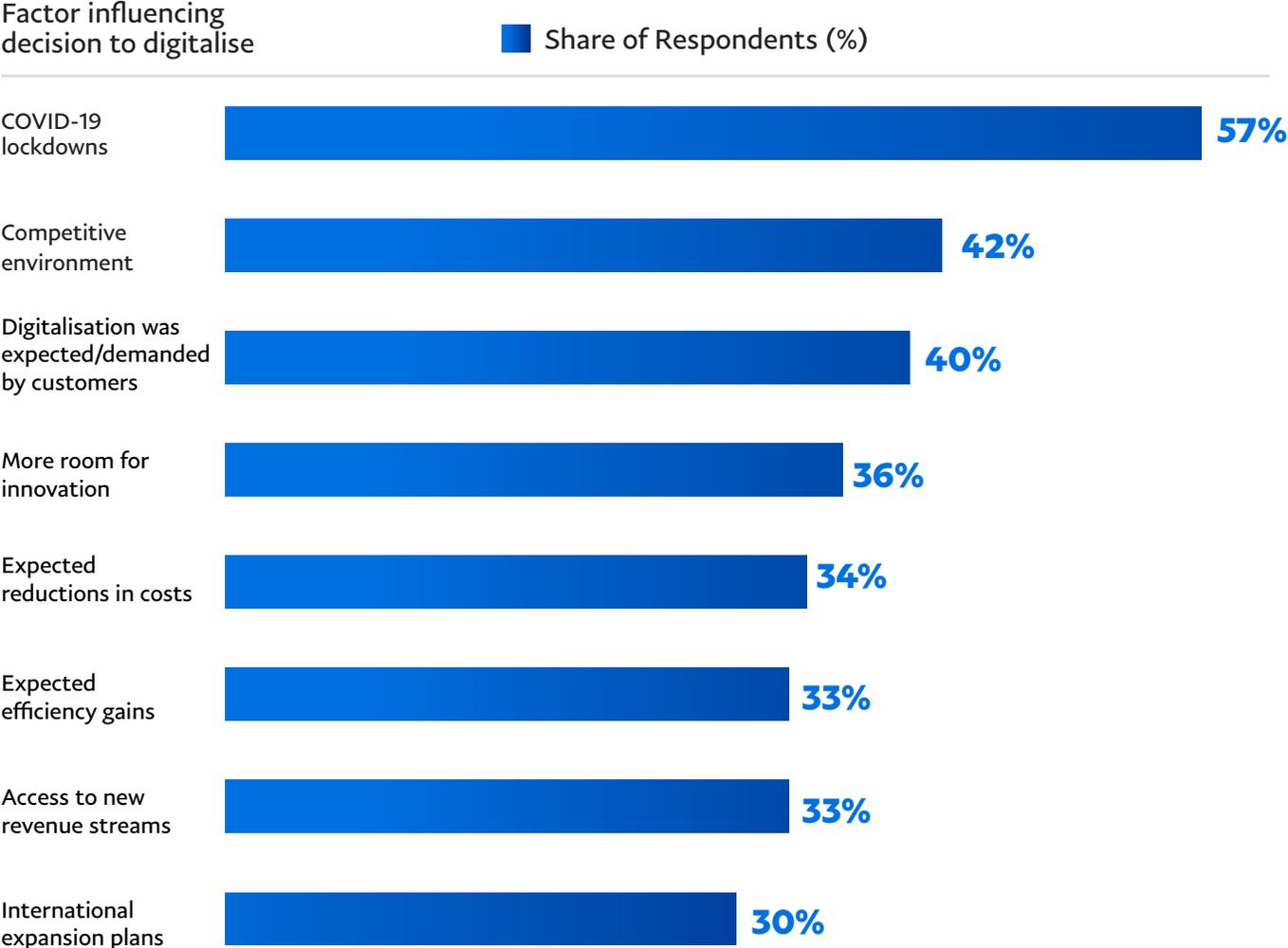
Areas of respondents' business that have been digitalised. (More than one option is allowed).



Prior to the pandemic, Malaysian businesses especially SMEs, were lagging behind the global average in digital adoption.²² However, prolonged lockdowns necessitated by the virus compelled businesses of all sizes in Malaysia to shift online. Amongst survey respondents, nearly 6 out of 10 (57%) businesses stated that COVID-19 lockdowns influenced their decision to digitalise their business. Other factors driving digitalisation include the competitive environment (42%), demand from customers (40%), scope for innovation (36%) and expected cost reduction benefits from digitalisation (34%) (See Figure 3).

Figure 3

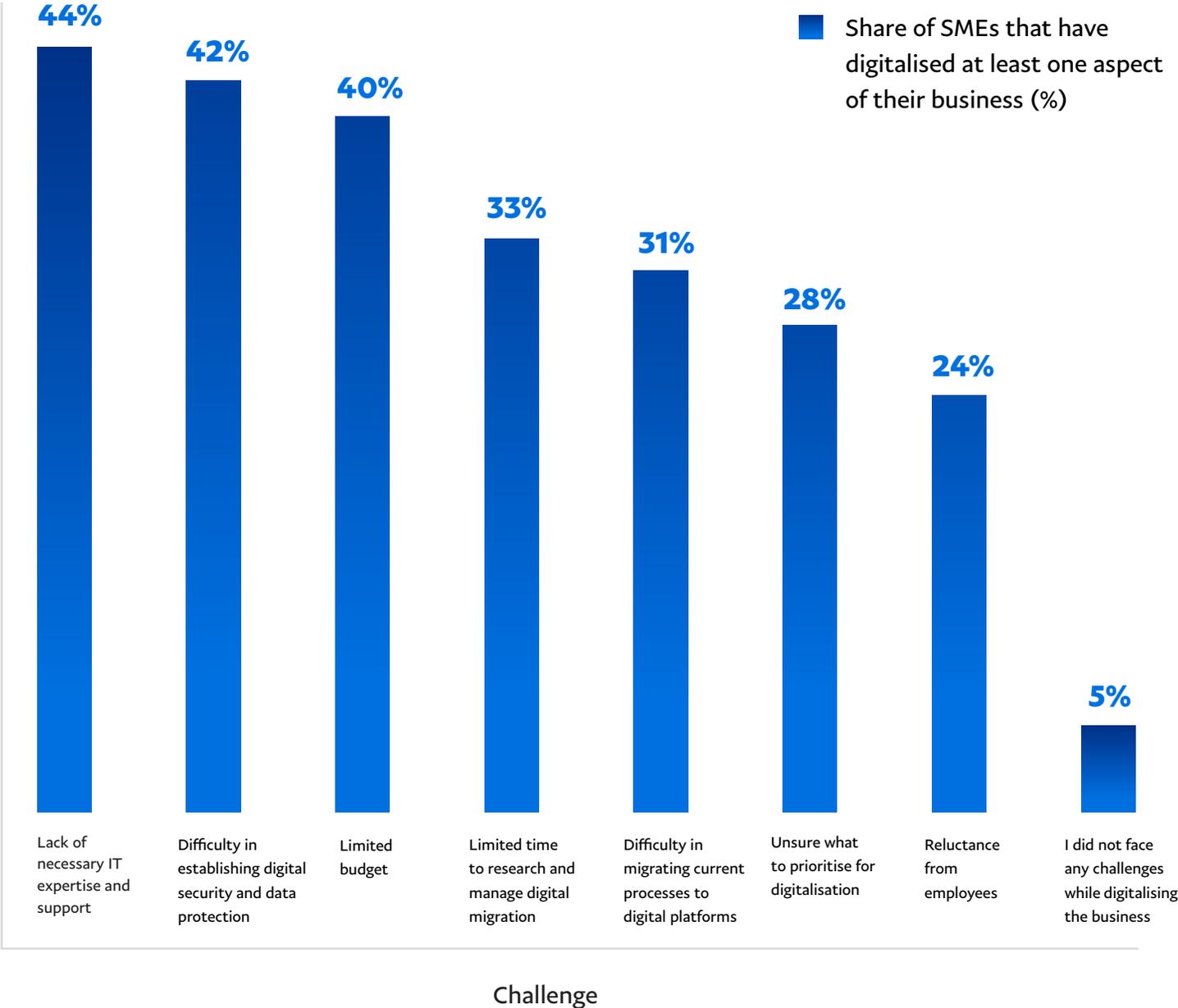
Factors driving digitalisation amongst Malaysian SMEs. (More than one option is allowed).



Realising these benefits through digitalisation has not been an easy task for a majority of the digitalised SMEs. Across the 936 SMEs that have digitalised at least one aspect of their business, only 49 businesses (5%) claimed to have faced no challenges in the process of digital transformation. All others faced challenges in digitalisation – 44% cited lack of necessary IT expertise and support as the most common hurdle, followed by difficulty in establishing digital security and data protection (42%), as well as budget constraints (40%). One-third of the sample said that they had limited time to research and manage digital migration while 28% were unsure about the areas of their business to prioritise in digital transformation (See Figure 4).

Figure 4

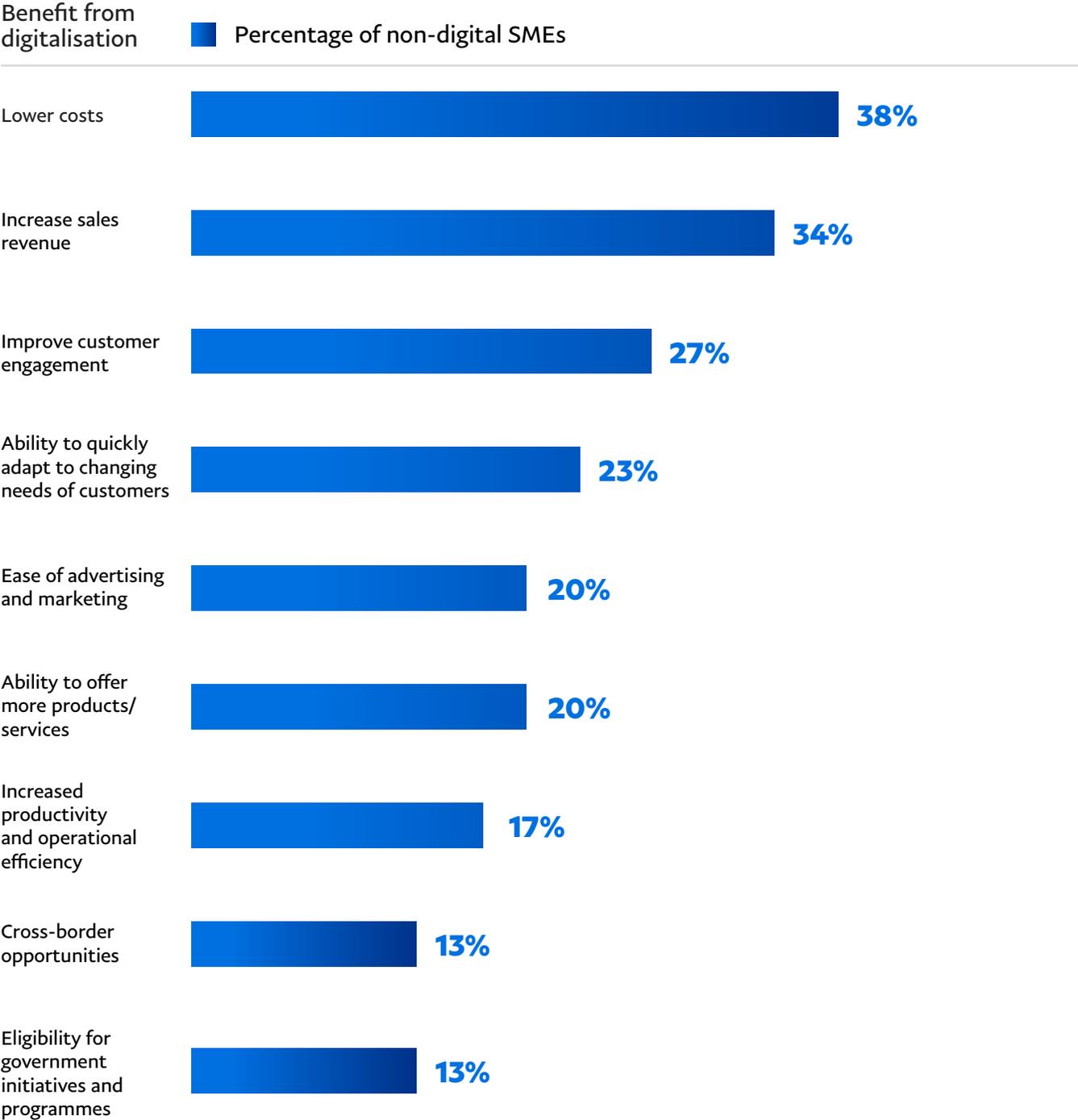
**Challenges faced by Malaysian SMEs in their digital transformation journeys.
(More than one option is allowed).**



For SMEs that did not embrace digitalisation, tangible benefits would be necessary to incentivise them to make the shift. For these businesses, the greatest incentive to digitalise would be reduced costs (38%) and increased sales (34%). Other compelling benefits are consumer centric: improved customer engagement (27%) and ability to adapt to the changing needs of customers (23%) (See Figure 5).

Figure 5

Benefits that would induce non-digital SMEs to undertake digitalisation. (More than one option is allowed).

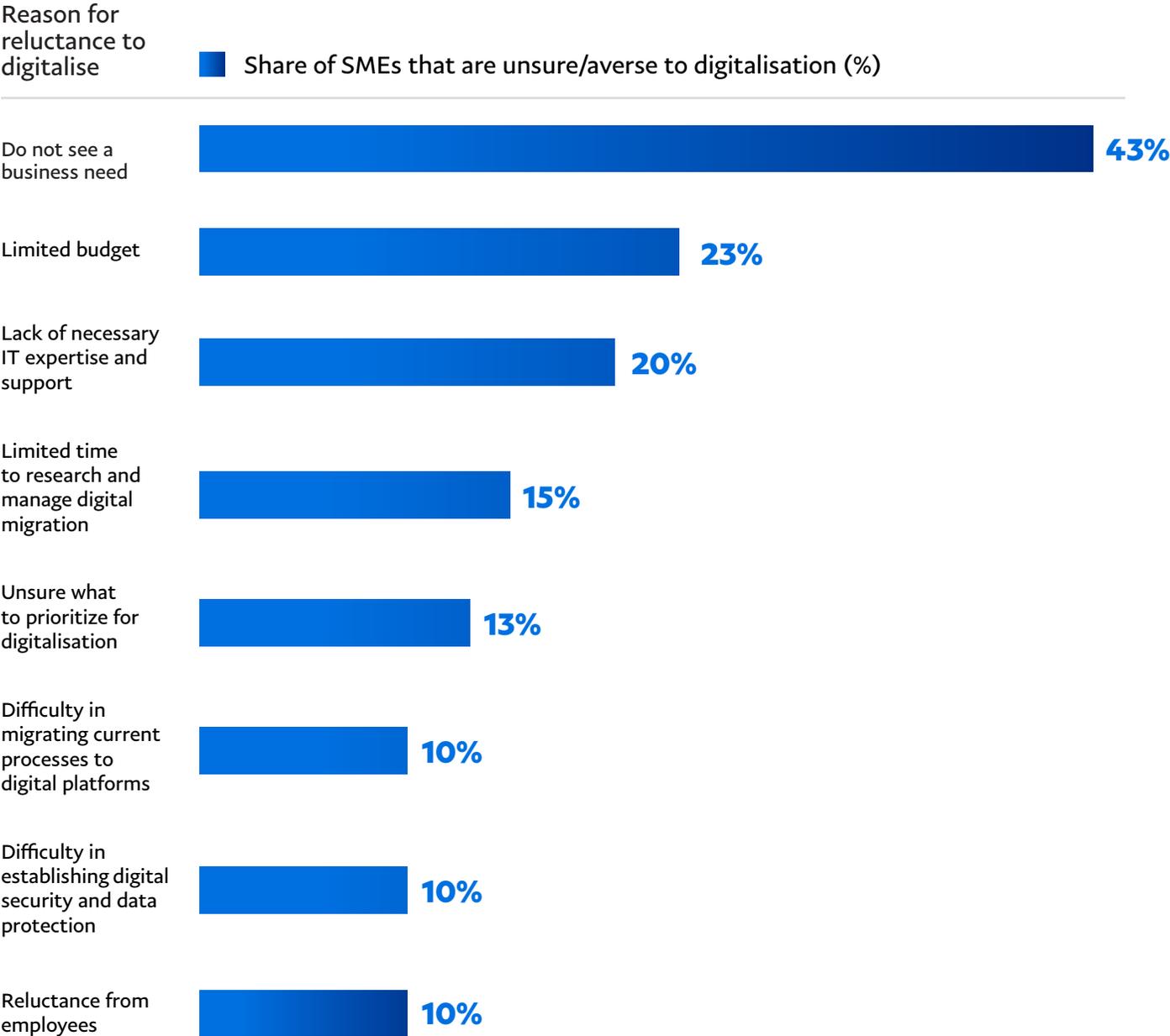


Amongst those who have not yet digitalised, 38% of them said that they would consider digitalising their business in the near future while 44% remain unsure and 19% said that they would not digitalise their business at all.

In these latter two groups, 43% said that they do not see a business need for digitalisation whereas nearly a quarter were held back by limited budgets, and one-fifth by lack of necessary IT expertise and support (See Figure 6).

Figure 6

Reasons why businesses are not considering or are unsure about digitalising their businesses in the near future. (More than one option is allowed).

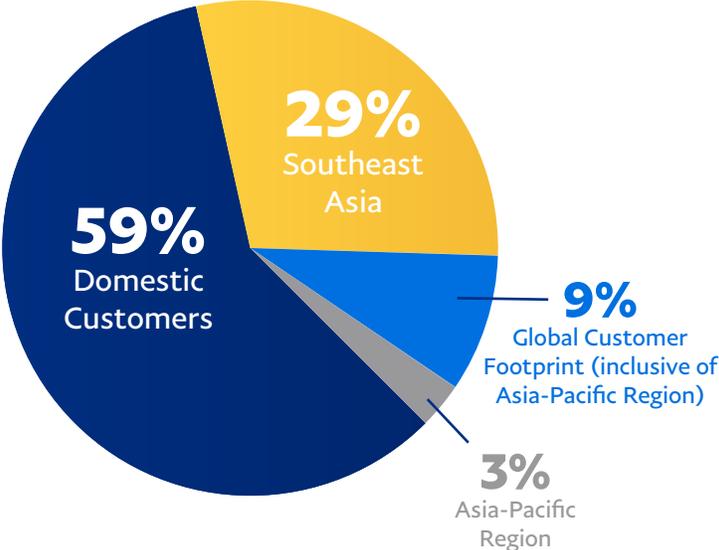


Cross-Border Trade and Internationalization

Cross-border trade has been a key driver of Malaysia's economic success. According to the World Bank, "Malaysia is one of the most open economies in the world with a trade to GDP ratio averaging over 130% since 2010. Openness to trade and investment has been instrumental in employment creation and income growth, with about 40% of jobs in Malaysia linked to export activities."²³ Malaysia's openness to the global economy has made it an economic powerhouse in the Southeast Asia region.

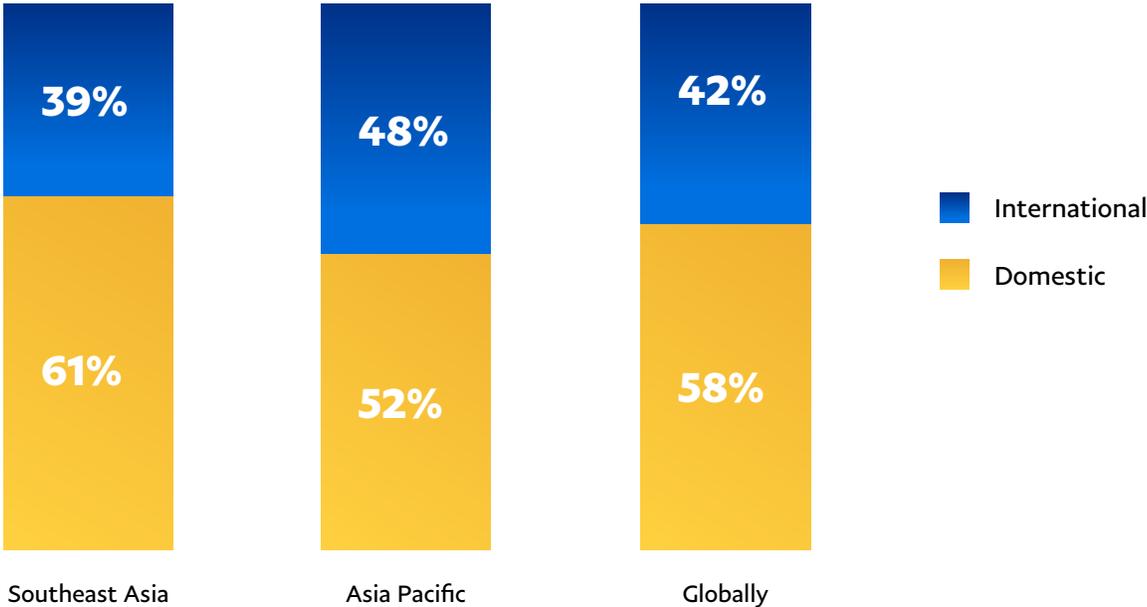
Our survey revealed that nearly 6 out of 10 Malaysian SMEs (59%) only sell to domestic customers. The rest are SMEs that sell internationally. 29% of SMEs sell to customers within Southeast Asia; 3% to customers in the Asia-Pacific region; and 9% have a global customer footprint (See Figure 7).

Figure 7
Malaysian SME Customer Locations



On average, SMEs who sell internationally derive 60% of their sales from domestic customers and 40% from international customers.²⁴ SMEs selling across the APAC region have the highest share of their turnover coming in from cross-border sales at 48%, compared to 39% across Southeast Asia and 42% globally (See Figure 8).

Figure 8
Domestic and International Shares of annual turnover



Location of Customers

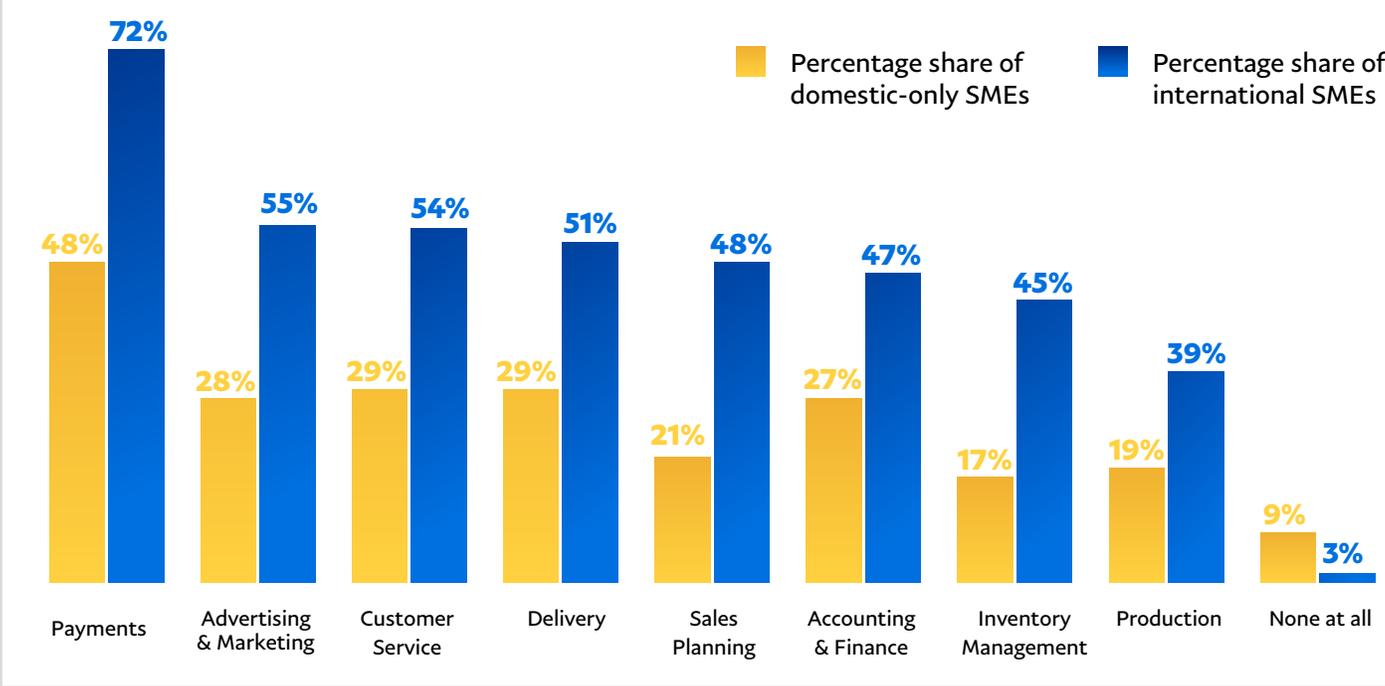
Selling internationally yields several benefits to Malaysian SMEs. A manufacturing SME that we spoke to in the interviews told us that margins are much better with international customers, as compared to those from domestic sales. Additionally, in niche sectors such as wellness, according to an SME in this sector that we spoke to, international customers are often more well-informed and discerning – and consequently, more willing to pay premiums for quality.

At the same time, it is clear that there is both regional and global demand for goods and services offered by Malaysian SMEs. Malaysia is a power player in the international Islamic economy – having ranked at the top of the Global Islamic Economy Indicator for the past nine years.²⁵ Malaysian SMEs are steadily building a global reputation in sectors such as modest fashion and have immense potential to cater to Muslims all over the world. The global modest fashion sector alone is valued at US\$295 billion and Malaysian SMEs have begun strong forays into the sector.²⁶ Similarly, Malaysia ranks fifth globally in the halal cosmetics industry, with the country contributing US\$3.6 billion of sales to a global estimated total of US\$70 billion.²⁷

Digitalisation is critical for the Malaysian SME sector to fulfil its tremendous potential. There is a clear correlation between digitalisation and internationalisation. Businesses that had digitalised aspects of their operations are more likely to sell internationally. For these businesses, payments are the foremost priority for digitalisation. For example, 72% of international SMEs have digitalised their payment functions compared to less than half of SMEs that sell only within Malaysia. Reliable digital payments providers deliver safe, secure, and fast transactions that enable sellers and buyers to transact with confidence across national borders (See Figure 9). For example, according to the findings of a 2019 study of multiple emerging markets on the PayPal platform, SMEs using PayPal surpassed others in export values and number of trade partners.²⁸

Figure 9

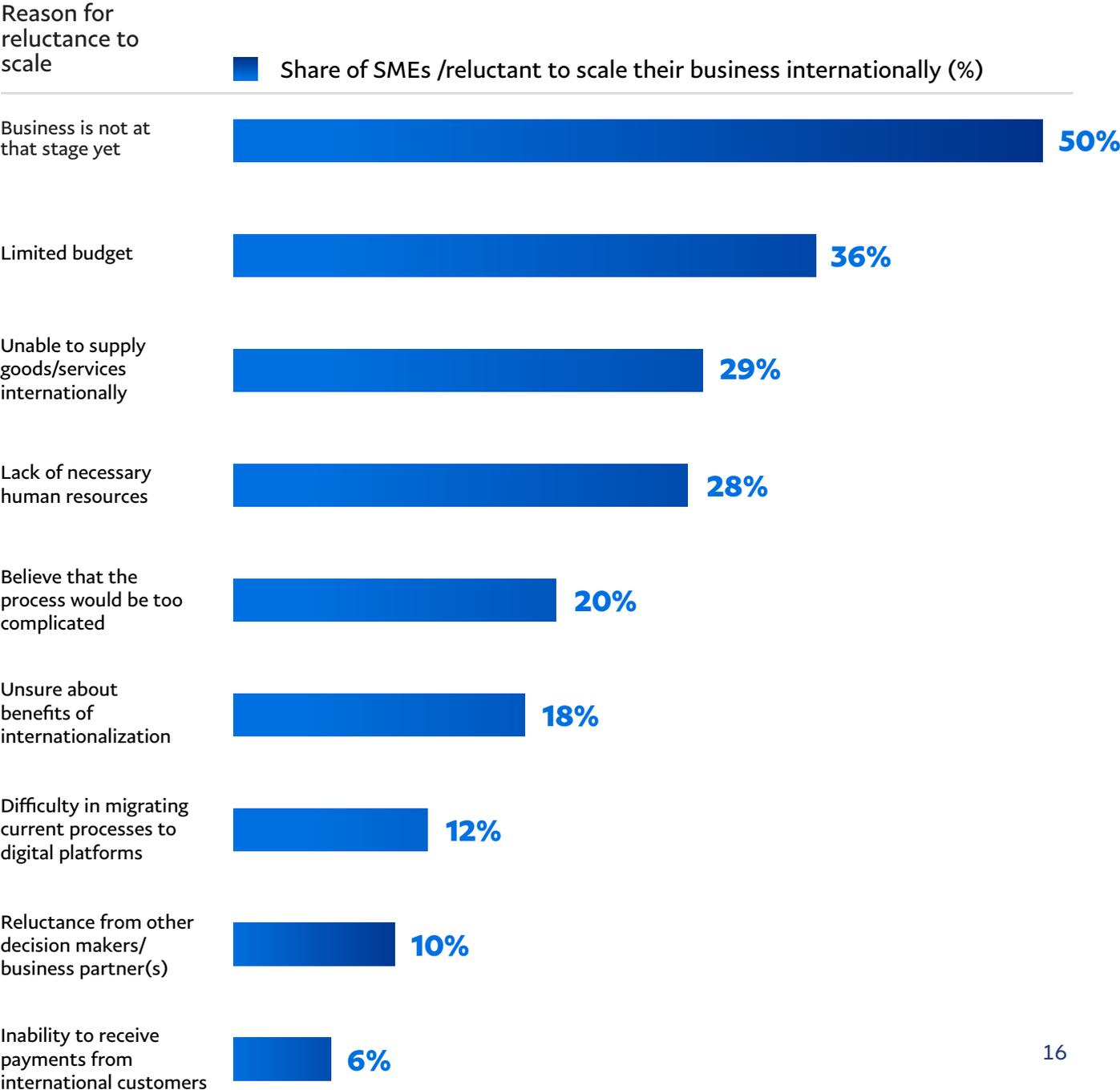
Priority areas of digitalisation of domestic-only and international SMEs. (More than one option is allowed).



Amongst the SMEs that currently only sell domestically, 61% hope to scale their business internationally in the near future while 17% are not considering cross-border sales at all and the remaining are unsure. Amongst those who are not intending to internationalise or are unsure about their plans to do so, half of the respondents said that they did not feel that their business is at the stage of internationalisation yet. Budget constraints (36%), inability to supply their products and services outside Malaysia (29%), and lack of human resources necessary for such internationalisation (28%) were also identified as major obstacles to cross-border business. At the same time, only 12% SME foresee difficulties with digitalisation and 6% found challenges in receiving payments (See Figure 10).

Figure 10

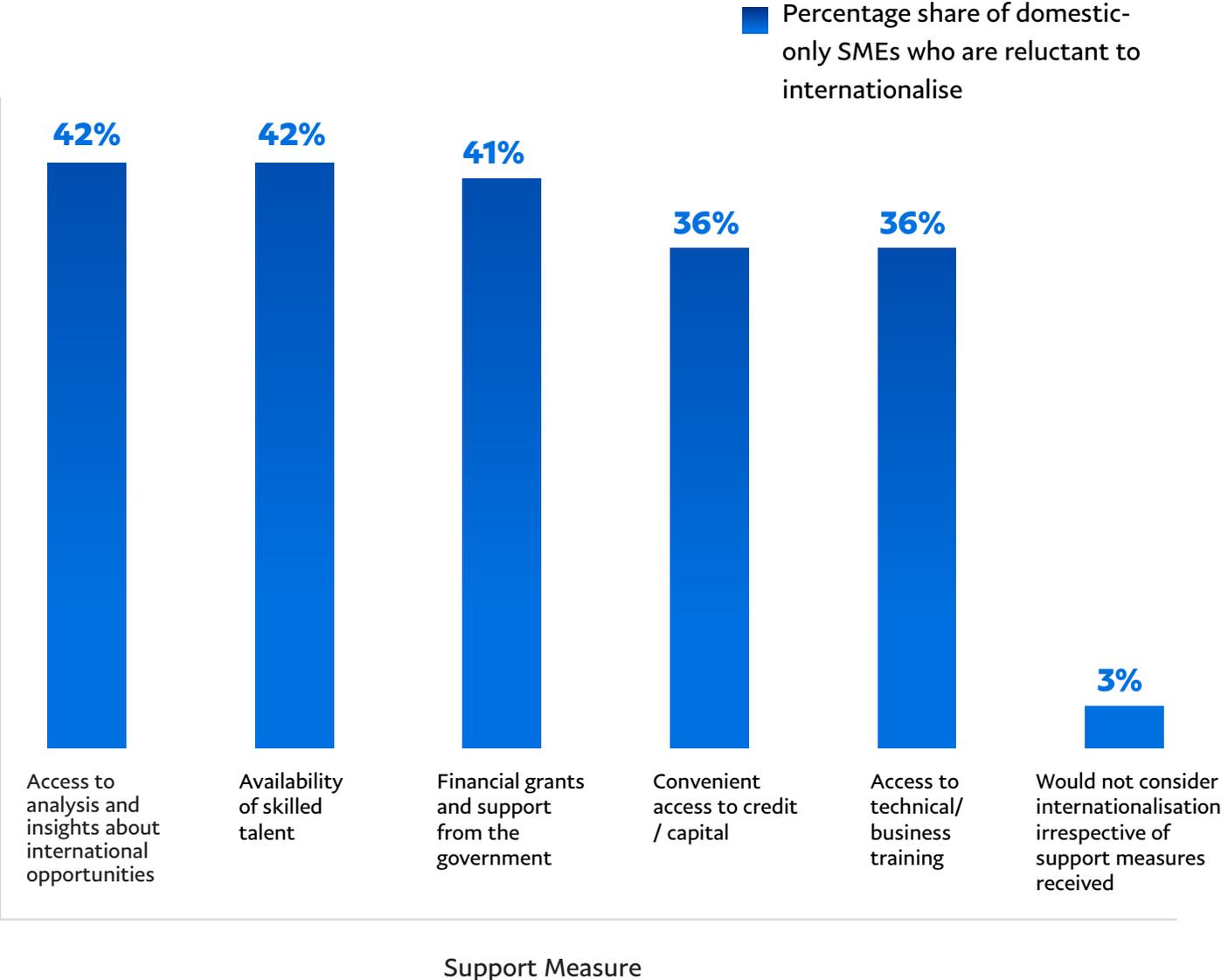
Reasons why the respondent was uncertain about/reluctant to scale their business internationally in the near future. (More than one option is allowed).



Amongst the 39% of domestic-only SMEs who remain uncertain or unconvinced about leveraging international opportunities in the near future, many feel that there are support measures that could be made available which would help them consider cross-border selling. 42% of this demographic want access to analysis and insights about international market opportunities that will help develop their business strategy. The share of those who feel that the availability of skilled talent would enable them to internationalise was also 42% while 41% believe they would be able to do so with financial grants and government support. Thirty six percent will need convenient access to credit/capital and an equal number require technical and business training to sell outside Malaysia. A small share of respondents (3% of those uncertain/unconvinced) said that they would not consider internationalisation at all irrespective of support measures or resources offered (Figure 11).

Figure 11

Support measures sought by SMEs to internationalise. (More than one option is allowed).



Digital Payments and Accelerating Digitisation

In this study, we defined digital payments in the survey as electronically enabled payment modes other than cash, cheques, physical credit/debit/ATM cards at point of sale, and cash on delivery. Based on this definition, a striking 92% of SMEs surveyed stated that they use digital payments.

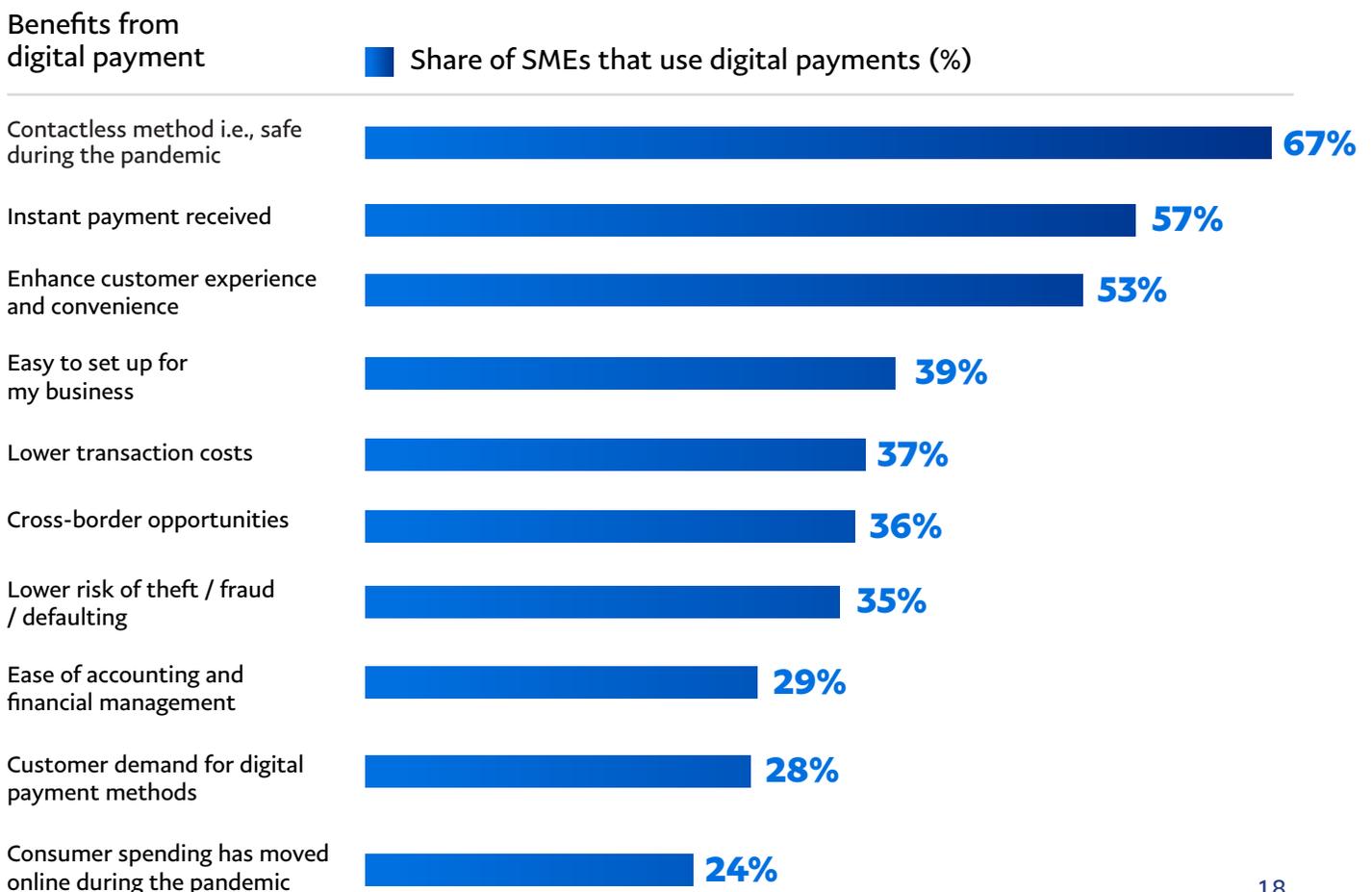
A striking 92% of SMEs surveyed stated that they use digital payments.

The majority of the SMEs (58%) we surveyed had prioritised payments in their digitalisation efforts. According to insights published by IDC, Malaysian SMEs' adoption of digital tools in the aftermath of the pandemic was driven by the need to be cashless. The Malaysian government's ePenjana initiative, which encouraged e-wallet use for safe, contact-free payment, was instrumental in driving adoption of digital payment by businesses and consumers.²⁹

Our survey shows that a large share of Malaysian SMEs has embraced digital payments and firmly believe in its benefits. The pandemic played a catalytic role in the adoption of digital payments with 67% of digital payment enabled SMEs stating that they did it for health and safety concerns. Other reasons were the immediacy of payment delivery (57%) as well as to enhance customer experience (53%) (See Figure 12).

Figure 12

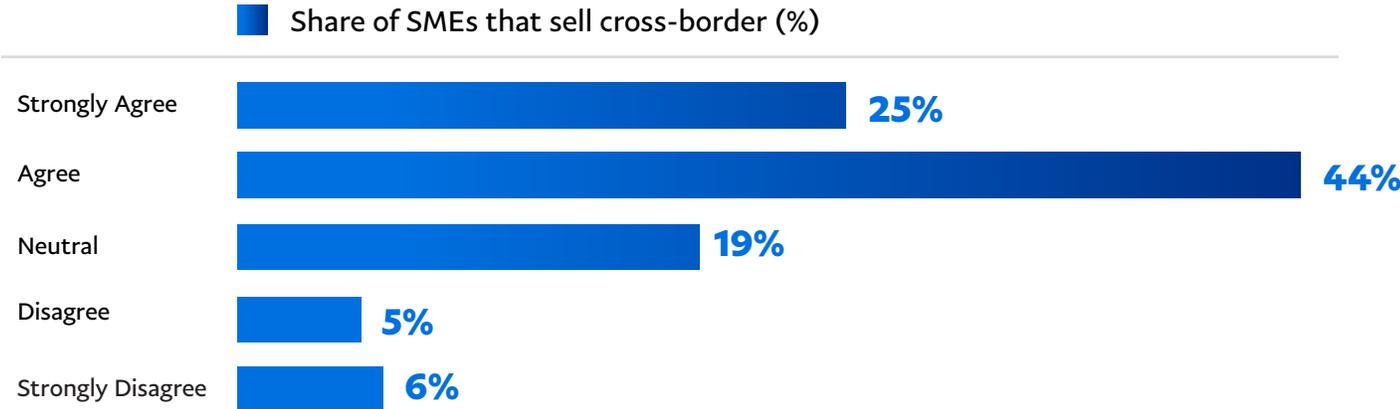
Reasons for choosing digital payments for business



Payments are a particularly important issue for cross-border businesses, with 7 out of 10 of these businesses agreeing that the digital payment options they have on offer influences the trust placed in them by their international customers (See Figure 13).

Figure 13

The digital payment options offered for my international customers influences their trust in my brand/business.

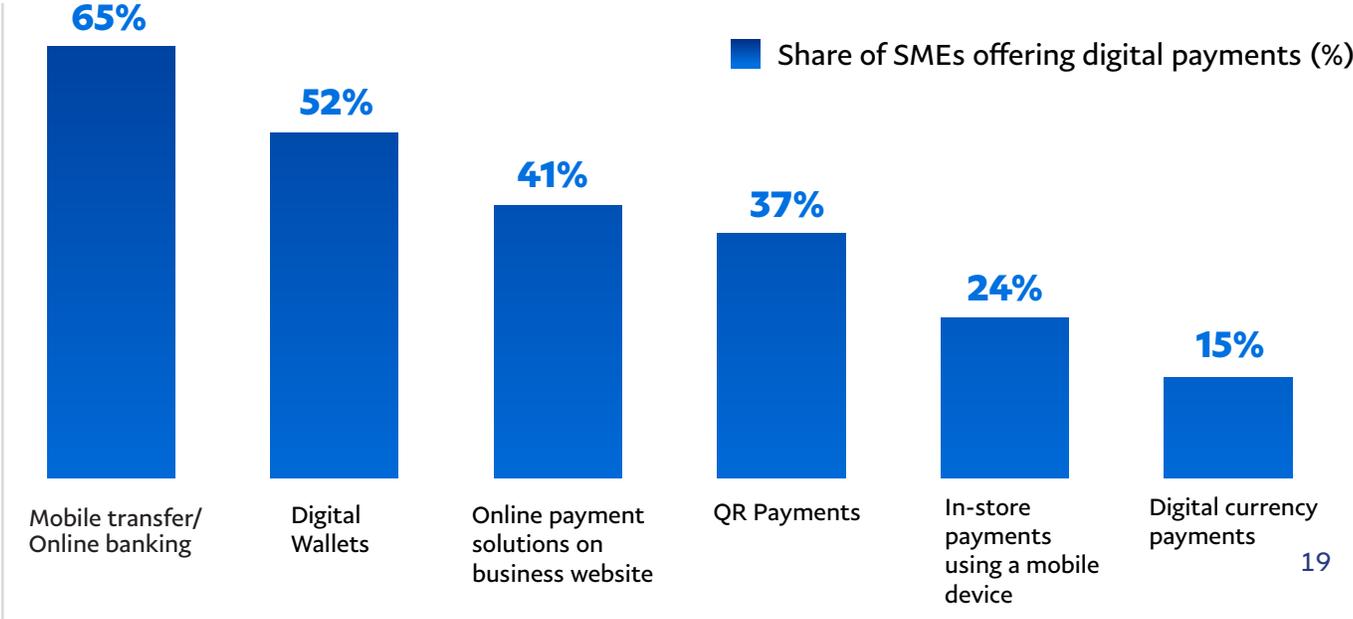


Additionally, through in-depth interviews with SMEs, we found that SMEs across the board appreciate the benefits of having diverse payment options on their website to cater to customers with varying preferences. For example, a bespoke Malay fashion SME stated that when it first integrated payment options into its new website in 2020, it decided to offer a variety of options for its customers to choose from in order to enable ease of transacting.

Malaysia currently has a slew of digital payment options available and most SMEs in our sample offer more than one option. Similar to other markets in the region, mobile transfers or online banking has emerged as a popular choice for receiving payments by SMEs, with 65% of the digital payment enabled businesses in our sample offering this mode of payment followed by 52% accepting payments through digital wallets (See Figure 14).

Figure 14

Digital Payment Modes by Popularity of Use amongst SMEs

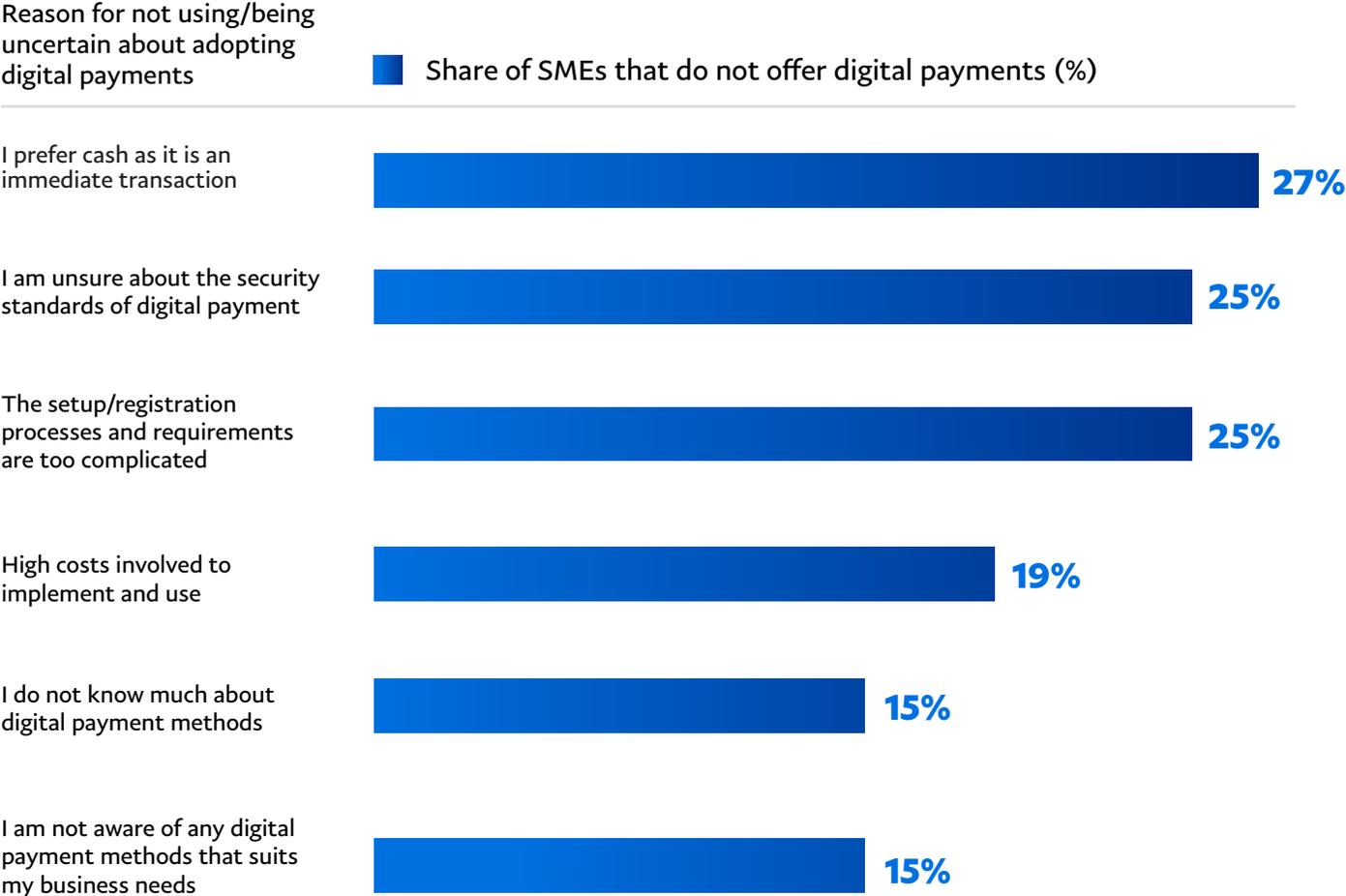


Digital payment mode

Amongst the SMEs who do not accept digital payments at the moment, 41% are considering doing so in the future, while 36% are unsure, and 21% are certain that they will not be adopting digital payments. In the latter two groups, the greatest deterrent from the adoption of digital payments is the immediacy of cash (27%) followed by uncertainty about the security standards of digital payments (25%) and frustration with the complicated setup and registration processes of current digital payment offerings (25%) (See Figure 15).

Figure 15

Reasons for discomfort with digital payments. (More than one option is allowed).



Recommendations

Based on the survey results and the insights they provide, there are five key recommendations for consideration and could accelerate SME's digitalisation in Malaysia:

- i. enable digital payments as a stepping stone towards comprehensive digitalisation;
- ii. enhance public-private collaboration could support the implementation of SME digital strategies;
- iii. empower women entrepreneurs in the digitalisation of SMEs;
- iv. provide training and workshop on cybersecurity; and
- v. enhance awareness and reach of government initiatives that support digitalisation.

1: Enable digital payments as a stepping stone towards comprehensive digitalisation

Digital payments can play an important role in digital transformation and can serve as a gateway to comprehensive digitalisation. Integration into a digital payment network or a payment platform enables SMEs to get comfortable with digital tools and gives them confidence in the benefits that digitalisation can bring to their businesses. Payment service providers can help with this process by working proactively with the government to increase adoption of their services and by removing barriers to access to their platforms that might exist.

According to SME Corp Malaysia, 77% of SMEs in the country remain only at the basic digitalisation stage. In our survey, while many SMEs have digitalised at least one aspect of their business – digitalisation has not been uniform. A small share of SMEs surveyed had digitalised key aspects of their business that would help boost productivity – such as inventory management, accounting and finance, and sales planning. Boosting the adoption of emerging new technologies such as AI and machine learning in operations management and sales planning can provide SMEs with significant increases in sales and productivity.³⁰

Many SMEs that want to but have not yet digitalised

Even SMEs that are completely non-digital in all other aspects of business have begun to accept and adopt digital payments.

express a sense of feeling overwhelmed by the multitude of digital software available and being uncertain about how to start their digital journey. Nevertheless, in our research, we found that even SMEs that are completely non-digital in all other aspects of business have begun to accept and adopt digital payments.

For instance, an SME owner we interviewed who runs a grocery business told us that though nearly all aspects of her business are non-digital – including customer payments which are only accepted in cash – 30% of payments to suppliers are made through online transfers. In addition, 92% of all respondents in our

survey told us that they accept some form of digital payments³¹ from their customers. This, coupled with the fact that 74% of Malaysian customers have been using e-wallets on average in one survey conducted by UOB, seems to confirm a trend that there is increased demand for digital payment options from customers, and SMEs who do not offer digital payment options might find themselves lagging behind as customers opt for the convenience offered by cashless payment systems.³²

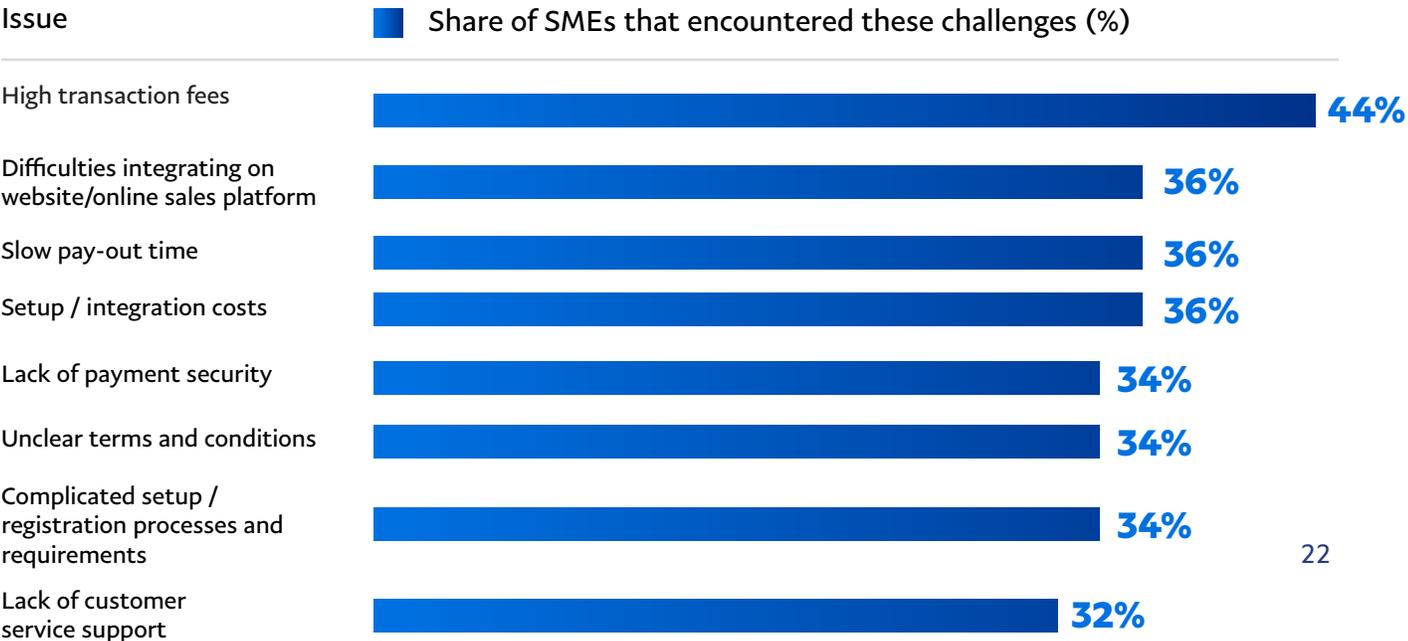
At the same time, governments, businesses, and customers across Southeast Asia have also embraced digital payments as the future of financial transactions. Many central banks in the Asia-Pacific region are at the forefront of innovations in payments and are working on new methods of cashless payments including central bank digital currencies (CBDCs) and instant payment systems.

Malaysian SMEs seeking to sell cross-border have to ensure that they adapt and evolve to provide international customers with secure and convenient payment options that these customers can trust. For example, according to a Borderless Commerce study conducted by PayPal in 2022, German shoppers have become increasingly comfortable with digital payments, so offering multiple secure payment options is paramount for global merchants in 2022. Today, the most popular online payment method for German shoppers is PayPal due to its security, quick payment processing, and convenience.³³ The study also found that for the Australian shopper, data privacy is top-of-mind. To win consumer trust, Malaysian SMEs can partner with leading payment brands that consumers trust with their sensitive data at checkout. For example, PayPal’s reputation for security and convenience has made it the most popular online payment methods in Australia for both domestic and cross-border purchases.

If digital payments indeed could be considered the stepping stone to comprehensive digitalisation, then it is crucial to help SMEs overcome the barriers to setting them up. In our survey, we asked Malaysian cross-border SMEs that have already undergone the process of selecting a digital payments platform for their international business about the barriers they faced. High transaction fees were cited as one of the greatest challenges that such SMEs face during setup, with 44% stating that this had been an issue for them. More than one-third of these SMEs (36%) faced difficulties integrating payments systems into their existing websites or online platforms. Other difficulties faced by these SMEs included slow pay-out time (36%), high setup and integration costs (36%), lack of payment security (34%), unclear terms and conditions (34%), and complicated registration processes and requirements (34%) (See Figure 16).

Figure 16

Challenges that SMEs face when setting up digital payments



Clearly, there are many opportunities here for the government and payment service providers to collaborate and resolve these challenges. For example, newly digitalised SMEs could get financial help for a fixed time frame at the beginning of their digital journeys to defray the set up costs; these could be in the form of subsidies from the government or rebates and discounts from service providers. To resolve technical difficulties and integration issues, step-by-step instructional videos which include information about customer service contacts could be created by payment providers and made readily available to SMEs by government agencies and small business advocacy organisations.

Payments can be the first step towards empowering SMEs with the knowledge and insights that will enable them to undertake a **strategic** approach to digitalisation. Payments and transaction data can be utilised to design a digitalisation strategy for businesses that take into account available resources and projected future sales. Transaction data on payment gateways can provide insights to SMEs on areas of their business to prioritise for additional investment and digitalisation. Public and private partners can come together to provide diagnostic tools and self-assessments to SMEs that would help identify their current needs and available resources as well as the digital tools and solutions required to fulfil both short-term and long-term goals. Even for SMEs that have already embarked on their digitalisation journeys, the ability to gain insights from their own transaction data can yield rich benefits. In our survey, 42% of domestic-only SMEs who are currently reluctant to internationalise stated that access to analysis and insights about international opportunities would enable them to sell cross-border. Additionally, one of our interviewees - a café owner from Selangor – said that when he thinks about digitalising his business in the next three to five years, his focus is on getting his “payment systems in order” so that he can leverage transaction data to analyse sales patterns, improve inventory management, and eventually make data-driven operational decisions including café hours. Government agencies such as Malaysia Digital Economy Corporation (MDEC) and SME Corp can also work with financial institutions to utilise payments and transaction data to provide credit and working capital support for SME digitalisation initiatives, even in the absence of traditional forms of collateral – thereby resolving the issue of funding constraints that preclude some small businesses from adopting digital tools.

2: Enhance public-private collaboration can support the implementation of SME digital strategies

Digital payments can help SMEs take the first step towards digitalisation and payments data can be leveraged in many different ways to provide additional support to SMEs in their digital transformation journey, including in the creation of a robust digitalisation strategy. However, the actual implementation of a digital strategy can seem challenging to SME owners – especially if they are not confident in their own digital acumen. This is where the public and private sector could collaborate and step in to support SMEs in their digitalisation strategy. In particular, we have identified five areas where enhanced public-private collaboration could provide added support.

First, the lack of IT skills and knowledge of SMEs,

which has been identified as one of the greatest obstacles to SME digital adoption globally.³⁴ Singapore’s Infocomm Media Development Authority (IMDA)’s Chief Technology Officer (CTO)-as-a-Service programme for SMEs is a good example of how enhanced public-private sector collaboration could serve SMEs.³⁵ The programme enables businesses to self-assess their digital needs and readiness from anywhere and at any time, to access proven and cost-effective technology solutions, as well as to connect with consultants with the technology and project managements expertise that would enable them to manage the process of digitalisation in a way that best fits their businesses.

Second, the public and private sectors, together with educational institutions could create guidebooks and resources on digitalisation for businesses. As the Malaysian SME ecosystem is much larger and more diverse than that of Singapore, similar efforts like the CTO-as-a-service programme would require deeper collaboration between the public, private, and educational sectors in Malaysia to have wide and meaningful impact. MDEC has launched several key initiatives to educate entrepreneurs in the country about digitalisation. In 2021, MDEC launched comprehensive SME Digital Guidebooks for the F&B and retail sectors that provide a strong foundation on which businesses in these sectors can build their digital futures.³⁶ The guidebooks provide information about key trends impacting these sectors, the benefits of digitalisation, as well as a step-by-step guide for SME digital acceleration. These are supplemented by case studies of Malaysian SMEs at various stages in their digital transformation journeys as well as details of the tools and technologies that they used to achieve their goals. As a resource, the guidebook provides important information for entrepreneurs seeking to understand how digitalisation could work for their business. The private sector and educational institutions can partner with MDEC to create similar guidebooks and resources for businesses in other sectors as well.

Third, by working closely with government agencies such as MDEC, the private sector, and institutes of higher learning, as well as industry bodies and groups can provide targeted technical and business support to SMEs through mentorship programmes, focussed workshops, and on-site or virtual digital clinics. AmCham Singapore's SME Accelerate initiative, which brings large multinational corporations and SMEs together to help small businesses is an example of a programme that brings a diverse range of stakeholders together to help SMEs devise solutions to their challenges with the help of mentors and experts from larger companies and technology solution providers.

Fourth, alongside education and training as well as mentorship and consulting services, the public and private sectors can also collaborate to build out a repository of proven software solutions that have benefited SMEs in Malaysia with specific issues. In

Singapore, IMDA's pre-approved directory of digital solutions has become an important reference point for SMEs seeking to digitalise. The government and technology solution providers can also come together to provide discounts and rebates on the costs of these solutions – especially during the first few years of adoption or for SMEs below a certain turnover threshold.

Lastly, other challenges faced by SMEs we interviewed were employee training and change management, where the government and private sector could share their expertise in business continuity and change management to help smooth out these processes. Resources and training on digitalisation should also include helpful guidance on managing the process as seamlessly as possible.

The public and private sectors can also collaborate to build a repository of proven software solutions that have benefited SMEs in Malaysia with specific issues.

3: Empower women entrepreneurs in the digitalisation of SMEs

Government agencies such as MDEC and SME Corp can partner to create dedicated SME digital support networks for women entrepreneurs across Malaysia and provide them with the resources and access to technical expertise and resources that will help their businesses digitalise. By creating a platform for women entrepreneurs to share best practices and to support each other in their digitalisation journeys, such an initiative could help identify specific pain points as well as tested solutions to ameliorate them.

The women entrepreneurs we interviewed highlighting several challenges such as a need to change societal perceptions, having to manage multiple familial responsibilities along with their businesses, as well as greater and more difficulties accessing credit compared to men.

With regards to social perception about women, one interviewee said that while the media features male entrepreneurs quite prominently and regularly, stories about successful women entrepreneurs are few and far between. According to her, more representation of success stories of women in business in the media can provide motivation and allay the fears of other aspiring entrepreneurs. The interviewee added that it is often difficult for women to secure a support circle that can enable them to stay motivated. This observation is in line with research conducted by the APEC which found that women-owned firms in Malaysia lag in formal networking,³⁷ which can deprive them of access to mentorship, market intelligence, and opportunities.

Another interviewee cited multiple familial responsibilities along with their businesses, leading to greater opportunity costs for attending multi-day workshops or other training events. Providing a platform for the emergence of a community where they can seek ad-hoc advice and guidance from their peers would significantly benefit women entrepreneurs and help them navigate challenging business environments.

Create dedicated SME digital support networks for women entrepreneurs across Malaysia.

More representation of success stories of women in business in the media can motivate and allay the fears of other aspiring entrepreneurs.

One interviewee also said that women-owned SMEs have more difficulties accessing credit than those owned by men. Digitalisation of businesses, by tracking existing sales and providing predictive data for future growth prospects, can help provide non-traditional metrics for credit scoring that can help SMEs prove their credit worthiness even without collateral. This is especially important for women as lack of collateral and financial documents have led to lower loan approvals to women entrepreneurs.³⁸ The government can work closely with payment service providers as well as digital credit platforms and accounting software providers to develop robust channels for SME credit that are directed particularly towards women.

Malaysia's share of women-owned businesses in Malaysia is low, especially when compared with its neighbouring countries.³⁹ According to the latest available data from the World Bank, the share of firms with female participation in ownership in Malaysia is only 25%. In comparison, this share is 69% in the Philippines, 64% in Thailand, and 51% in Vietnam.⁴⁰ The ratio is much lower amongst SMEs. According to 2019 data (latest available official figure) from SME Corp, only 20% of Malaysian SMEs are owned by women.⁴¹ Although the 2021 Malaysia Gender Gap Index report revealed that women had surpassed men in the educational attainment sub-index in recent years,⁴² higher education has not led to a corresponding expected increase in entrepreneurship as women still face steep challenges including social expectations,⁴³ difficulties in securing credit due to complex loan application processes,⁴⁴ as well as perceived low levels of government support.⁴⁵ An APEC study of women SMEs in Malaysia, Thailand and The Philippines also found that women entrepreneurs lagged behind men in technology adoption.⁴⁶



Citation: smecorp.gov

Empowering women entrepreneurs in their digitalisation efforts of their firms can help to address these issues and lead to greater gender parity, which is in turn is a key driver of economic growth. According to Cuberes and Teignier (2016), Malaysia's entrepreneurship gender gap of 71% (estimated by the authors), is creating an average income (GDP per capita) loss of 6%.⁴⁷ Therefore, all stakeholders interested in the growth and prosperity of Malaysia have a vested interest in enabling the development and success of women entrepreneurs in the country.



**Malaysia's
entrepreneurship
gender gap of 71% ,
is creating an
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per capita) loss of 6%**

Citation: Cuberes and Teignier (2016)

Along with these near-term initiatives, forward-looking measures that promote technology education is vital to help Malaysia attain the GDP gains that are currently lost to the entrepreneurship gender gap. According to the Malaysian Human Resources Development Corporation, even though women represent the majority of university graduates in the country, they are still underrepresented in Science, Technology, Engineering, Mathematics and Computer Sciences (STEM).⁴⁸ In the long term, focussed collaborative efforts by the public, private, and educational

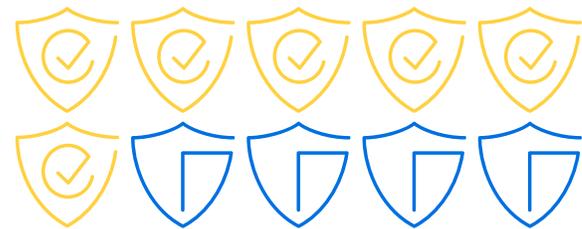
sectors that empower more women to pursue higher education and careers in STEM can help create future generations of entrepreneurs with the skills to deploy the right digital tools for their businesses.

4: Provide training and workshops on cybersecurity

In the PayPal survey, the second most cited challenge amongst those who had digitalised their businesses was concerns about cybersecurity and data protection with more than 4 in 10 (42%) of all digitalised SMEs saying that they encountered difficulties in this area. At the same time, SMEs are more vulnerable to cyberattacks and are specifically targeted by malicious actors.⁴⁹

According to data published by the Ministry of Communications and Multimedia Malaysia (KMM), 84% of SMEs in Malaysia have been compromised by cyber threat incidents and 76% of small businesses have suffered more than one attack.⁵⁰ In response, KMM has developed and implemented a cyber resiliency programme called Matrix Cybersecurity for SME (Matrix), utilising “a three-pronged strategy to mitigate and prevent instances of cyberattacks.

Alongside this laudable initiative, the government can work with various private and public sector stakeholders to ensure that cybersecurity is a key component of any program targeted at SMEs. Many SMEs in the country are hesitant to embark on the digitalisation journey because of concerns about cybersecurity. It is therefore important to empower SME owners and decision makers to feel confident that the digitalisation strategy they choose will help protect customer and financial data from breaches and that they will know the right response measures to undertake in the event of a cyberattack. This is especially important as more than a one-third of the SMEs we surveyed – 38% - currently do not have any cybersecurity measures in place. While it is reassuring that 23% of SMEs are looking to adopt cyber defence measures in the near future, 15% have no plans to do so. Only slightly more than one-third of the respondents – 34% - have dedicated cybersecurity personnel on staff and the remaining 28% rely on automated cybersecurity solutions (See Figure 17).



More than 42% of all digitalised SMEs encountered difficulties with cybersecurity and data protection

SMEs are more vulnerable to cyberattacks and are specifically targeted by malicious actors.

Ensure that cybersecurity is a key component of any programme targeted at SMEs.

84% of SMEs in Malaysia have been compromised by cyber threat incidents



76% of small businesses have suffered more than one attack

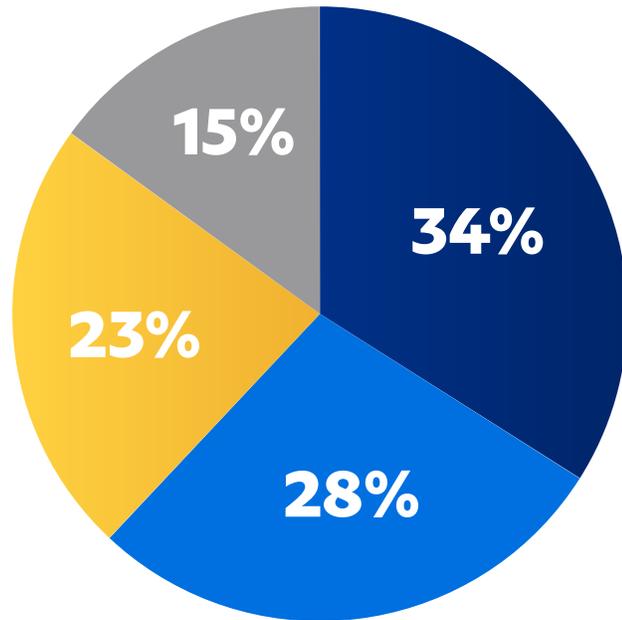


Citation: kkmm.gov

Figure 17

SMEs approach to cybersecurity

- I have a dedicated employee(s) to monitor all cybersecurity activities
- I rely on automated cybersecurity solutions
- I do not have any cybersecurity services, but I would like to adopt some in the near future
- I do not have any cybersecurity services and I am not looking to adopt any anytime soon



These findings are also in line with the results of a [2021 PayPal study of ASEAN FinTech firms](#) which found that a majority of them (61%) could not find cybersecurity talent to fulfil their cybersecurity compliance requirements.⁵¹ MDEC's NxFORCE programme, which trains students in cyber defence with an aim to develop the next generation of cybersecurity professionals⁵² offers an excellent conduit of cyber talent that SMEs can draw from. By incorporating an SME-traineeship component in NxFORCE, MDEC can provide hands-on training to participating students in tackling real-world cyber issues while also helping small businesses meet their cybersecurity talent needs.

Additionally, the 2021 PayPal study also found that compliance is a driving factor in ASEAN firms' cybersecurity decision-making. However, small businesses often face difficult decisions in resource allocation and cybersecurity compliance can pose an additional challenge to their digitalisation efforts due to the high costs of breaches and of regulatory non-compliance in handling or protecting customer data. As identified in the PayPal ASEAN FinTech Cybersecurity Matrix, government-provided funding devoted to helping companies strengthen their cybersecurity capabilities can aid resource-crunched SMEs invest in cyber resilience and protect against breaches and resultant financial losses.

An important step towards enabling these entrepreneurs who rely on externally provided cyber defence systems is for the government to provide a directory of trusted vendors and service providers with reliable cybersecurity credentials. Such a repository of proven software solutions can allay fears while also providing SMEs with a range of vendor choices suited to their needs. Additionally, the government can institute clear guidelines for SMEs of all sizes in the event of a breach so that business owners do not feel helpless in the event of a cyber incident.

5: Enhance awareness and reach of government initiatives that support digitalisation

Despite efforts by the government to support digitalisation, many Malaysian SMEs are unfortunately still unaware of them. Hence, the Malaysian government could consider stepping up its proactive engagement with SMEs through promotion and outreach via diverse outlets, such as social media, industry groups, technology solution providers as well as local community organisations.

In 2019, Malaysia announced SME digitalisation as a key priority and in the government’s 2020 Budget, the SME Digitalisation Grant scheme was created to support businesses seeking to digitalise.⁵³ Thereafter, with the conceptualisation and release of the Malaysia Digital Economy Blueprint and allied efforts, much progress has been made in digitalising businesses of all sizes across Malaysia.

Despite these positive strides, however, more than a quarter of SMEs – 28% - remain unaware of digitalisation programmes and initiatives carried out by the government. Amongst those who were aware of government initiatives and support programmes, only 65% had participated in such programmes for their own business. At the same time, a large share of these SMEs that had taken advantage of such government initiatives (71%) said that they found these programmes to be helpful for their business, while 19% said that these initiatives had no significant impact, and only 10% said that such initiatives were unhelpful (See Figure 18). Given that a vast majority of the SMEs have benefited from these programs, it is important that continued and sustained efforts are made to promote these resources and to ensure that they are accessible and utilised.

Our interviews revealed that many SMEs are not aware of government support programs for SMEs. When asked whether they had received any assistance or grants from the government to support their business more broadly, one SME responded, “Is there government support out there?” She went on to elaborate that she had thought of support from the government as something only given to “those who were jobless” and that other SME owners in her network were not aware of such initiatives.

Another SME owner said that when she first wanted to set up her business, she had sought financial assistance from various government agencies, but the lengthy documentation and processes required as well as the long waiting time for decisions led to her withdrawing funds from her Amanah Saham Bumiputera (ASB) funds in order to meet setup costs for her business. Aside from lack of awareness about government initiatives and hesitancy due to previous difficulties in applying for assistance, more than one SME also voiced concerns that applying for such grants could bring them under additional scrutiny or interference by the government while others stated that they simply did not have the time to explore the various schemes available and their eligibility criteria.

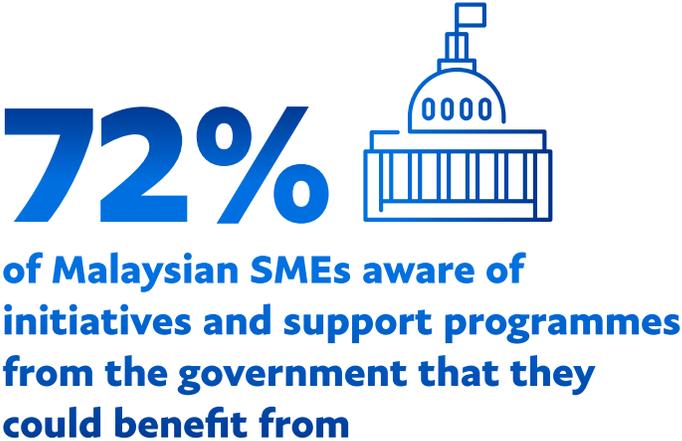
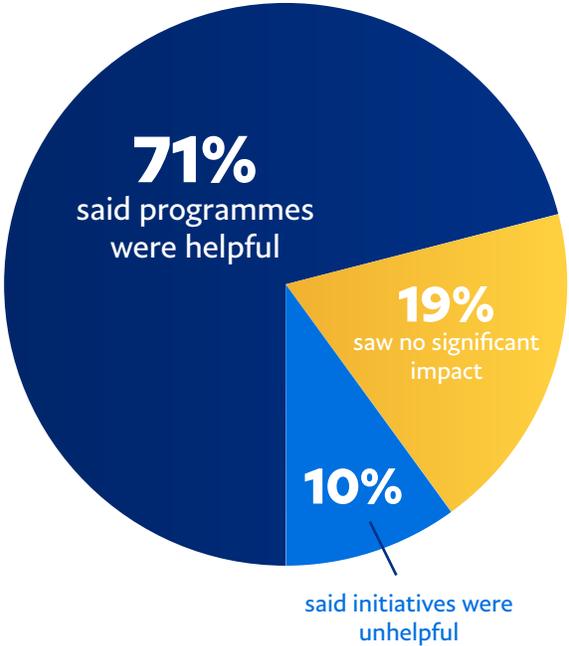


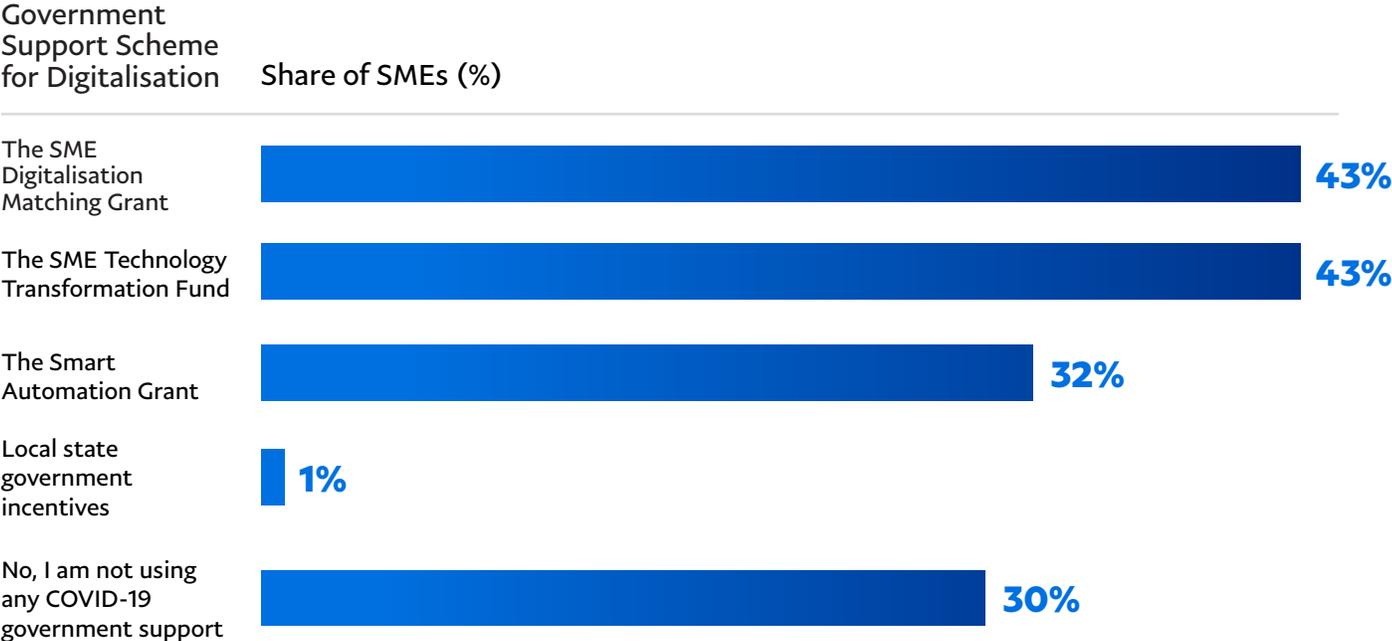
Figure 18
Were government digitalisation initiatives and support programmes helpful?



Despite targeted efforts by the government during the pandemic and extensive media reporting about the grants and assistance available to SMEs to digitalise, 30% of all SMEs in our sample had not taken advantage of any COVID-19 government support grants or initiatives to implement digitalisation (See Figure 19).

Figure 19

Adoption of COVID-19 government support used for digitalisation of business. (More than one option is allowed).



Even the best and most well-intentioned government initiatives for SME digitalisation can only achieve their desired impact if business owners are aware and utilise them. Thus the government may wish to step up its engagement with SMEs. For example, organisations like SMECorp and MDEC can work together to create a grants and programmes finder akin to the web tool that has found great success in Australia.⁵⁴ The Grants and Program finder on the Australian Government’s business support website (www.business.gov.au) has a user-friendly interface that enables small businesses to navigate and easily identify resources best suited to their needs.

Another important avenue for outreach to business is through technology solution providers. One of our interviewees told us that he became aware of his eligibility for the SME Digitalisation Matching Grant offered by MDEC through a vendor that he had engaged for SEO services. By working closely with

vendors and technology providers that serve SMEs, the government can ensure that eligible SMEs can receive the financial support and other assistance to successfully carry out digital transformation.

Even the best and most well-intentioned government initiatives for SME digitalisation can only achieve their desired impact if business owners are aware and utilise them.

Conclusion

SMEs are the foundation of the Malaysian economy. Their digitalisation is essential to Malaysia's post-pandemic economic recovery and long-term growth. Digitalisation is not a one-step process and there is no one-size-fits-all approach that SMEs can adapt to realise the benefits and opportunities of new technologies. Enabling SMEs to digitalise holistically and in a manner that is suited to their business needs and goals would help them maximise their turnover while also getting the highest returns on any investments made towards digitalisation.

While SMEs in Malaysia have made great strides in their digitalisation journey, concerted efforts by the government, larger private sector firms, and educational and other non-profit institutions can help tackle the challenges that are holding the Malaysian SME sector back from realising the full benefits of digital transformation. In this study, PayPal provided a snapshot of the Malaysian SME sector and the state of its digitalisation efforts in the aftermath of the pandemic. Additionally, this report also identified five key recommendations as suggested by our survey results and analysis, and support measures from a diverse range of stakeholders to accelerate the digitalisation of the Malaysian SME sector. In particular, the role of digital payments can play in providing a stepping stone towards comprehensive digital transformation for small businesses. With concerted efforts by the ecosystem, new opportunities will enable Malaysian SMEs to survive and thrive in the growing digital economy.

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About PayPal

Fueled by a fundamental belief that having access to financial services creates opportunity, PayPal is committed to democratizing financial services and empowering people and businesses to join and thrive in the global economy. PayPal has remained at the forefront of the digital payment revolution for more than 20 years. Our open digital payments platform gives PayPal's over 429 million active account holders the confidence to connect and transact in new and powerful ways, whether they are online, on a mobile device, in an app, or in person. Through a combination of technological innovation and strategic partnerships, PayPal creates better ways to manage and move money, and offers choice and flexibility when sending payments, paying or getting paid.

Available in more than 200 markets around the world, the PayPal platform enables consumers and merchants to receive money in more than 100 currencies, withdraw funds in 56 currencies and hold balances in their PayPal accounts in 25 currencies.

For more information on PayPal, visit <https://www.paypal.com/about>

About InsightzClub

InsightzClub is a tech-driven consumer insights firm that provides intelligent and actionable insights to consumer brands to make data driven decisions. InsightzClub works with customers across various industries such as FMCG, BFSI, Media, Education, Telco and many more.

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