Small firms should also think global

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China's State Administration of Taxation very recently and very publicly reported that the value-added tax, or VAT, reforms introduced earlier this year have reduced the tax burden incurred by China's army of small businesses by 40.6 billion yuan ($6.57 billion). The administration also noted that a total of 1.29 million of China's small businesses have been helped by these reforms.

This is indeed welcome news, especially at a time when domestic consumption and the growth of smaller Chinese companies are pivotal to China's economy.

But will tax savings necessarily lead to a more competitive, innovative and market-oriented Chinese small business sector? And will tax savings encourage China's small businesses to venture overseas and climb the internationalization ladder more quickly and effectively?

Sadly, the answer to both of the questions above is a resounding and unequivocal "no". Cost savings in any shape or form are beneficial, particularly to smaller companies with their vulnerability to the slightest vicissitudes of economic turbulence. But the benefits are only really realized with careful investment.

Even now with Europe's woeful economic picture, it is still Germany and the German economy that remain strongest and most respected. Fundamental to Germany's economic power is, and has been, the internationalization of its small and medium business sector. Larger German companies such as Bayerische Motoren Werke AG, known as BMW, and Adidas AG dominate the media coverage but it is the army of market-oriented and internationally driven smaller German organizations that forms the bedrock upon which economic strength has been built.

Over recent years, an increasing number of Chinese companies have expanded overseas with increasing success. Huawei Technologies Co Ltd, ZTE Corp, Zhejiang Geely Holding Group Co Ltd and Lenovo Group Ltd have all risen to international prominence, often through cross-border takeovers. However, China's army of smaller companies - estimates put this number at about 40 million - remain conspicuous by their absence from the international business environment.

Sino-foreign business link-ups also continue to increase across mainland China, yet the vast majority of these also do not involve China's smaller business community.

VAT savings should, therefore, be used as the catalyst to promote rapid internationalization among smaller Chinese firms. Small business leaders need to establish clear objectives for tie-ups with foreign firms, both in pursuit of greater market share domestically and overseas.

If China's small-business sector is going to rival Germany's success then close, symbiotic business relationships with foreign firms are essential.

Research studies usually identify three key success factors behind the internationalization of small firms: effective networking, management motivation and low psychological distance. In my experience, spanning some 20 years, with China's smaller business contingent, it is the latter of these three that represents the greatest obstacle to international success.

An ethnocentric mind-set and lack of confidence lie behind the poor international showing of China's smaller firms. If overseas expansion is occasionally considered at all, and even more rarely carried out, China's smaller companies opt for those countries believed to be similar in national and business culture, that is with low psychological distance. The Middle East and Africa are, therefore, often prime targets. While these markets will allow China's firms to expand and internationalize to a degree, such strategies will not result in any substantial and sustainable change in competitiveness and business culture.

Expansion into Europe, particularly Northern Europe and North America, will lead to a far greater learning experience for China's small businesses. While this will also prove more difficult, it is certainly achievable. At present, for example, many European and US smaller companies will welcome capital injections and other support Chinese companies can offer.

China's small-business leaders need to focus on VAT savings but also re-configure "VAT" from value-added tax to vision and attitude transformation. This should then begin a fundamental change in their approach to expansion into Europe and the United States.