



The role of government connectivity in fostering innovation activities at small and medium-sized enterprises in Vietnam

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ABSTRACT

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This paper examines how government relationships influence the innovation activities of small and medium-sized enterprises (SMEs) focusing on the specific aspects of innovation impacted by these relationships. Additionally, it looks at the challenges, opportunities, and strategies that SMEs face in securing government contracts which are often vital for their growth. The research adopts a qualitative approach, collecting data through 121 questionnaires and 34 semi-structured interviews with SME leaders and owners in Hanoi, Da Nang, and Ho Chi Minh City. The findings indicate that government ties significantly affect various innovation aspects, including business models, organizational structures, processes, product development, services, branding, and customer engagement. Government contracts provide SMEs with valuable opportunities for business expansion and growth offering both financial support and strategic advantages. The study concludes that SMEs with strong government relationships tend to innovate more broadly and effectively, leveraging these connections to enhance competitiveness. In terms of practical implications, the research highlights the importance of building and maintaining strong government relationships as the key strategy for SMEs aiming to improve their innovative capacity. It also provides valuable recommendations for policymakers, suggesting the development of supportive public procurement policies and programs to help SMEs thrive through innovation. The findings offer useful insights for businesses and local authorities working to create an environment that fosters SME innovation and growth.

Contribution/Originality: The research explores the role of government connections in shaping the innovation practices of Vietnamese SMEs. It highlights how these relationships influence daily operations and long-term strategic decisions. The study offers unique insights into the impact of government ties on SME innovation by surveying key participants in three major cities.

1. INTRODUCTION

Innovation within enterprise operations has emerged as a compelling area of study for researchers, national policymakers, and corporate leaders (He & Tian, 2018). At the national level, innovation serves as a cornerstone of economic progress driving growth and development (Aghion & Howitt, 1992; Grossman & Helpman, 1991; Jones,

1995). At the enterprise level, innovation has been empirically shown to enhance operational performance and enterprise value, generating profits and fostering sustainable competitive advantages. This effect is particularly pronounced in highly competitive markets characterized by various enterprises and increasingly diverse consumer preferences (Artz, Norman, Hatfield, & Cardinal, 2010; Hirshleifer, Hsu, & Li, 2013; Hsu, Lee, Liu, & Zhang, 2015; Rosenbusch, Brinckmann, & Bausch, 2011; Sorescu & Spanjol, 2008).

Beck (2013) highlighted that 95% of enterprises worldwide are classified as micro, small, and medium-sized entities (SMEs). Studies focused on identifying the factors that influence the innovative activities of SMEs can yield valuable insights for both governments and businesses. A deeper understanding of these factors enables policymakers to design and implement targeted policies that foster enterprise innovation, thereby contributing to broader economic growth. Furthermore, such insights equip managers with the knowledge needed to strengthen innovative practices within their organizations.

Research on enterprise innovation has brought in significant attention. However, studies on the impact of government connections on enterprise innovation remain limited (Tsai, Zhang, & Zhao, 2019). In the context of Vietnam, no study has yet comprehensively explored the effect of government relationships on the internal innovative activities of enterprises. This paper examines how government relationships impact enterprise innovation and identifies specific types of innovative activities that may be affected by these relationships. Additionally, we aim to investigate the challenges, opportunities, and efforts faced by government-connected enterprises in securing government contracts from their perspective. In this research, we suggest solutions to enhance government support for innovation in SME, especially by utilizing government contracts as a mechanism.

2. THEORETICAL FRAMEWORK

2.1. Innovation

Innovation is defined as the creative synthesis of extant knowledge and resources (Huse, Neubaum, & Gabrielsson, 2005). It is expressed through a range of activities, such as launching new products or services, adopting new production methods or implementing innovative organizational structures (Damanpour, 1991). In today's competitive business environment, innovation is broadly acknowledged as a key driver in determining organizational success, especially under increasing competitive pressures. A substantial body of research has demonstrated that innovation positively influences enterprise performance and enables enterprises to establish sustainable competitive advantages (Herrera, 2016; Hirshleifer et al., 2013; Sorescu & Spanjol, 2008). Consequently, innovation has become a focal point of interest for academic researchers and enterprise managers.

In this study, we adopt the innovation model developed by Deloitte Development LLC (2015) to examine how government connections influence specific innovative activities within enterprises. This model categorizes innovation activities into three distinct groups which are as follows: (1) core activities, which pertain to internal operations. (2) Product innovation. (3) Customer experience innovation. Core activities encompass profit-generating models, partner relationships, organizational structures, and operational processes. Product innovation includes advancements in core products and services as well as associated offerings. Customer experience innovation comprises enhancements in customer service, distribution channels, branding, and customer care and engagement.

2.2. Government Connection

The concept of government relationships is delineated through two distinct perspectives. The first perspective posits that an enterprise possesses a government relationship when it exhibits government ownership as exemplified by state-owned enterprises where the government exerts influence over the appointment of key personnel (e.g., the chairman or manager being a government official) or when at least one significant shareholder is affiliated with the government (Cull, Li, Sun, & Xu, 2015). The second perspective frames government connection as a collaborative economic relationship with the government, encompassing enterprises that currently hold or have

previously executed contracts with governmental entities (Qi & Nguyen, 2021). For this research, we adopt the latter definition to investigate the influence of government connections on the innovative endeavors of small and medium-sized enterprises (SMEs).

Existing literature on the relationship between government relationships and enterprise innovation presents varied perspectives and findings. Hou, Hu, and Yuan (2017) argue that enterprises benefiting from government ties supported by governmental incentives and reduced market competition may pursue overinvestment leading to inefficient resource allocation for innovative activities. Conversely, other researchers argue that such government linkages foster innovation through multiple mechanisms. Tsai et al. (2019) suggest that enterprises with government affiliations gain privileged access to policy-related information enabling them to enhance their business strategies and operational innovations. Similarly, Qi and Nguyen (2021) emphasize that government connections facilitate access to funding, such as government grant programs or bank financing, creating a supportive environment for innovation.

In Vietnam, promoting innovation and entrepreneurial startups has emerged as a key policy focus in recent years. Decision No. 884/QĐ-TTg, issued on May 18, 2016 together with related policy documents demonstrates the Vietnamese government's strong commitment to advancing innovation and entrepreneurial ventures. This initiative specifically aims to establish a conducive ecosystem that encourages and sustains enterprise innovation. Furthermore, the government has set an ambitious goal to support 2,000 innovative projects and 600 innovative enterprises by 2025 reflecting a clear strategic focus.

In this paper, we hypothesize that government relationships are likely to exert a positive influence on the innovative activities of small and medium-sized enterprises (SMEs) in Vietnam. Based on this hypothesis, we establish three subsequent research objectives which are elaborated upon in the introduction and methodology sections.

3. RESEARCH METHODOLOGY

3.1. Research Design

This study adopts a qualitative research methodology to examine several key dimensions: (1) whether government relationships enhance the innovative activities of SMEs in Vietnam. (2) Specific innovative activities within SMEs are influenced by government connections. (3) The advantages and challenges SMEs encounter in securing and executing government contracts. (4) The ambitions and endeavors of SMEs in their pursuit of government contracts. The focus of this paper is to delve into the perceptions and perspectives of SMEs concerning the interplay between government connections and their internal innovative activities. A qualitative approach is deemed particularly appropriate for this investigation given the paucity of prior research on these topics within the Vietnamese context.

To realize these research objectives, we undertook two empirical studies. In the initial one, we administered a survey to ascertain whether government connections influence the innovative activities of SMEs in Vietnam and to gauge the willingness of Vietnamese SMEs to engage in government contracts. This preliminary study was designed to inform the direction of the subsequent investigation by collecting data through semi-structured personal interviews. Structured questionnaires were deemed an appropriate tool to optimize time, reduce costs, and secure a broader response pool compared to in-depth interviews. The second one constitutes the core of this research. Data for this phase were gathered through semi-structured interviews which facilitated a detailed exploration of the target groups outlined earlier. In the conducted interviews, participants were provided with questions in advance. Nevertheless, interviewers maintain the discretion to modify questions in response to contextual subtleties unique to each respondent or to introduce additional questions to elucidate or elaborate on responses. This interviewing approach is particularly appropriate to this study, given its novel focus and its intent to deeply investigate the viewpoint of SMEs.

3.2. Data Collection Process

The authors selected Vietnam's three largest cities Hanoi, Da Nang, and Ho Chi Minh City to conduct surveys and semi-structured interviews. Representing the northern, central, and southern regions of Vietnam, these cities encompass a wide range of SMEs operating across multiple industries. This selection ensures that the findings from these locations provide valuable insights for government agencies at various levels with applicability extending beyond these cities to other regions across the country.

For the first study, data were collected based on the snowball sampling technique. Survey questionnaires were sent to enterprise owners and departmental managers through personal referrals with participants subsequently encourage to share the survey with other appropriate contacts.

For the second study, the data collection process involved two phases. The first phase involved selecting respondents based on criteria relevant to the study, and the second phase involved interviewing respondents. In the first phase, respondents were selected based on two criteria: (1) They were the owners/CEOs or senior managers of SMEs (with less than 200 employees) and (2) the enterprises with government connections (they had previously undertaken contracts with local authorities or government).

The data collection for the second study unfolded in two phases: respondent selection and interviews. In the first phase, participants were chosen based on two criteria: (1) They were owners/CEOs or senior managers of SMEs (defined as enterprises with fewer than 200 employees). (2) Their enterprises had government connections evidenced by prior contracts with local authorities or government bodies.

Respondents were identified through referrals from personal networks and screened by telephone to confirm alignment with the target group criteria. Following this process, 34 suitable respondents were selected - 19 from Ho Chi Minh City, 11 from Hanoi, and 4 from Da Nang. During the initial phone contact, we obtained consent to schedule in-person interviews at locations deemed comfortable, quiet, and convenient by respondents, such as cafes with private spaces or their offices. The interviews were conducted by members of the research team.

Prior to each interview, respondents received a brief overview of the research team, the study's objectives, and assurances of confidentiality. Permission was sought to record and take handwritten notes during the sessions. However, respondents permitted only handwritten notes, precluding audio recordings due to the sensitive nature of topics related to government connections. Consequently, comprehensive handwritten documentation was employed throughout the interview process. To accommodate this requirement, each interview involved two researchers: one led the discussion using pre-prepared questions and noted key points from responses while the other recorded the full interview in writing, occasionally posing additional questions to elaborate on responses as needed. Interviews averaged approximately 30 minutes in duration. Following the initial interview, questions were refined and supplementary prompts were incorporated for subsequent sessions. Post-interview, the handwritten notes were transcribed into typed documents with key points extracted and stored separately to streamline data processing and analysis.

3.3. Data Analysis

For the first study, survey responses were coded in Excel to generate descriptive statistics, including business location, years of operation, SME size, and participants' positions. We calculated the percentage of enterprises expressing a desire for government connections and the proportion affirming a link between government connections and their innovative activities.

In the second study, interview responses were segmented and analyzed by question groups. Beyond general inquiries about respondents and their SMEs, four distinct question clusters aligned with the study's objectives: (1) the impact of government connections on SME innovation. (2) Specific innovative activities influenced by government connections. (3) Advantages and challenges in securing and fulfilling government contracts. (4) SMEs' aspirations for accessing government contracts. Responses were organized in Excel in both detailed and

summarized formats. Each question group's answers were then synthesized and examined in depth to determine the existence of a relationship between government connections and SME innovation, the types of innovation spurred by government contracts, the benefits and obstacles faced in pursuing and executing such contracts, and SMEs' ambitions regarding government contract opportunities. These insights enable the research to propose actionable recommendations for enhancing SME contract fulfillment from the perspectives of both local authorities and government bodies.

4. ANALYSIS AND DISCUSSION

4.1. Survey Results

Out of 121 processed responses, 71 responses (58.7%) came from Ho Chi Minh City, 31 responses (25.6%) from Hanoi, and 19 responses (15.7%) from Da Nang. Regarding the position of the survey respondents, 53 responses (43.8%) came from SME owners, 35 responses (28.9%) from senior managers, and 33 responses (27.3%) from middle managers. 35 SMEs operated for less than 5 years (28.9%), 43 SMEs operated from 5 to 10 years (35.5%), 28 SMEs operated from 10 to 15 years (23.2%) and 15 SMEs operated for over 15 years (12.4%). Regarding SMEs size, 19 businesses had less than 10 employees (15.7%), 48 businesses had 10 to less than 50 SMEs (39.7%), 24 SMEs had 50 to less than 100 employees (19.8%), and 30 SMEs had 100 to less than 200 employees (24.8%).

Among the 121 surveyed SMEs, 88 (72.7%) had previously fulfilled contracts with local authorities. 6 expressed reluctance to pursue further government contracts, citing concerns over complex and rigid acceptance procedures, multi-tiered approval processes, protracted negotiation periods entailing high costs, frequent regulatory changes, and a lack of transparency in certain information. Of the 33 SMEs that had never engaged in government contracts, 25 indicated a willingness to pursue such opportunities in the future while 8 had neither explored nor intended to bid for contracts with local authorities or government entities (see Figure 1).

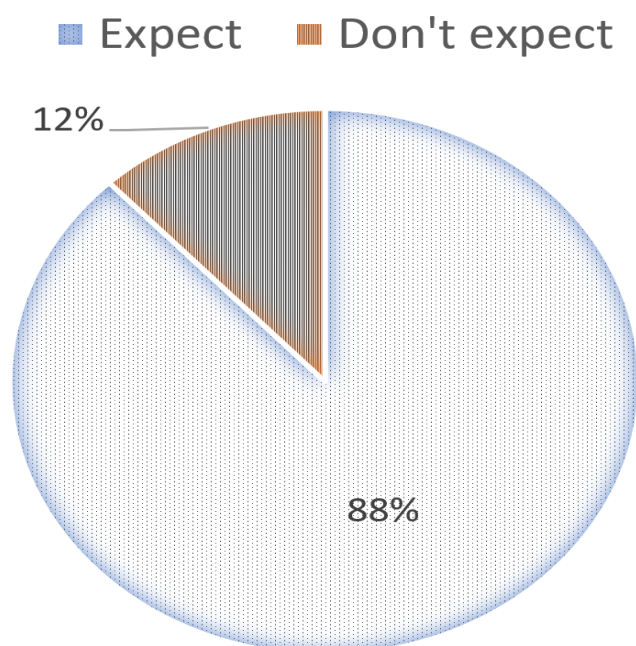


Figure 1. Expect to sign contracts with the government from the perspective of enterprises.

Out of 88 SMEs that had fulfilled contracts with government agencies, 68 SMEs agreed that innovations during the contract fulfillment process stemmed from government contracts. 11 SMEs believed that government connection partially impacted their innovative activities and 9 SMEs did not perceive any relationship between government connection and their innovative activities (see Figure 2).

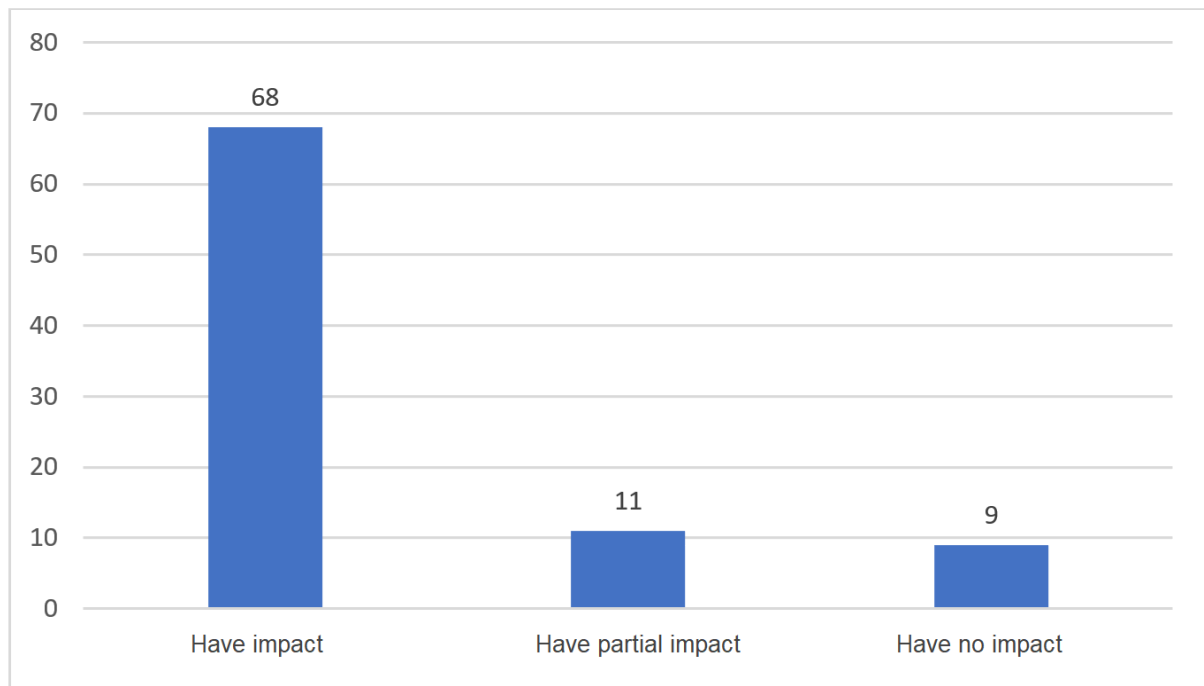


Figure 2. Impact of government connection on an enterprise's innovation.

4.2. Discussion of Survey Results

The survey findings indicate that government contracts hold significant potential to stimulate innovative activities among small and medium enterprises (SMEs) in Vietnam. Moreover, the results suggest that SMEs perceive government agencies as viable partners in their business endeavors. The advantages and obstacles SMEs face in securing and executing government contracts and the underlying motivations for their interest in partnering with government entities; a follow-up study involving in-depth interviews with SMEs is deemed necessary to substantiate these findings and gain deeper insight into the specific innovative activities spurred by government connections. The outcomes of these interviews are elaborated below.

4.3. Interview Results

4.3.1. Impact of Government Connections on SMEs Innovation

Among the 34 SMEs interviewed, 28 affirmed that their connections with government entities had a discernible impact on their innovation efforts, 2 reported a partial influence and 4 perceived no linkage between government contracts and their innovation initiatives. Illustrative responses include

- “It does have an impact because we have to innovate our processes to align with the changing regulations from the government (respondent 1).
- We have opportunities to reach more new customers, including opportunities to fulfill contracts with other government agencies. Therefore, government contracts are a motivating factor for innovation (respondent 6).
- Before these contracts, we were already a reputable supplier of quality goods and services, so we were innovating frequently. When we signed contracts with local authorities, we continued to innovate (respondent 17).
- These innovations aren't related to this contract but come from the SMEs' need to improve and innovate to increase production capacity and save costs (respondent 2).

The majority of interviewed SMEs confirmed a positive relationship between securing government contracts and their engagement in innovative activities.

4.3.2. Which Innovative Activities are affected by Government Connections?

The research team applied the [Deloitte Development LLC \(2015\)](#) to analyze responses from participants who recognized a connection between government ties and their innovation efforts to assess how government contracts influence SME innovation. According to [Table 1](#), government contracts serve as a catalyst across all categories of innovative activities within SMEs with pronounced effects on profit generation models, partner networks, core products or services, ancillary services, customer service, and customer engagement and care. This influence arises because government agencies represent a distinct client type for SMEs, necessitating compliance with specific requirements to secure contracts or succeed in government tenders. Furthermore, fulfilling contracts with local authorities affords SMEs opportunities to forge new partnerships and customer relationships, access capital and government support initiatives, and pursue broader business expansion and strategic development.

- We have an opportunity to expand our customer base and acquire many new customers. Networking is crucial; joining a potential network like this opens up numerous opportunities for us (respondent 10).
- We have to improve our products to meet the requirements of government agencies (respondent 13).
- The company gets additional contracts such as upgrades, maintenance, minor renovations, and maintenance of sound system equipment. As mentioned earlier, we are a reputable SME, so we are always innovating at every stage (respondent 17).
- Expanding relationships with the government is an opportunity not only for this contract but also for accessing other contracts, programs, partners, customers potentially even information and capital (respondent 20).
- Fulfilling the contract well builds reputation, trust, and capability for the company to continue winning other bids. Our brand is also elevated and we are innovating (respondent 29).

Table 1. Government relationship impact on an enterprise's innovation activities unit: Respondent (RP).

| Profit | Connection | Enterprise structure | Operation | Core products/ Services | Related products/ Services | Customer service | Distribution channel | Brand | Customer care |
|--------|------------|----------------------|-----------|-------------------------|----------------------------|------------------|----------------------|-------|---------------|
| RP1 | RP1 | | | | | | | | |
| RP6 | RP6 | RP17 | RP4 | RP5 | RP6 | RP4 | RP1 | RP5 | RP6 |
| RP7 | RP7 | RP21 | RP8 | RP6 | RP7 | RP6 | RP8 | RP6 | RP7 |
| RP8 | RP8 | RP30 | RP9 | RP7 | RP8 | RP7 | RP10 | RP8 | RP8 |
| RP9 | RP9 | | RP14 | RP8 | RP10 | RP8 | RP17 | RP11 | RP10 |
| RP10 | RP10 | | RP17 | RP10 | RP11 | RP16 | RP18 | RP14 | RP11 |
| RP13 | RP11 | | RP19 | RP11 | RP13 | RP17 | RP19 | RP17 | RP13 |
| RP14 | RP13 | | RP23 | RP13 | RP14 | RP19 | RP26 | RP19 | RP14 |
| RP16 | RP16 | | RP28 | RP16 | RP16 | RP20 | RP34 | RP20 | RP16 |
| RP17 | RP17 | | RP32 | RP17 | RP17 | RP25 | | RP22 | RP17 |
| RP18 | RP20 | | RP33 | RP18 | RP18 | RP30 | | RP29 | RP18 |
| RP19 | RP22 | | | RP19 | RP20 | | | RP31 | RP19 |
| RP20 | RP25 | | | RP27 | RP24 | | | RP32 | RP20 |
| RP27 | RP32 | | | RP28 | RP26 | | | | RP22 |
| RP29 | RP33 | | | RP29 | RP27 | | | | RP25 |
| RP32 | RP34 | | | RP32 | RP31 | | | | RP30 |
| RP34 | | | | | RP32 | | | | RP32 |

4.3.3. Advantages and Challenges in Accessing and Fulfilling Government Contracts

Respondents highlighted that a key advantage of pursuing government contracts is the public availability and accessibility of tender information, disseminated through various channels. SMEs with prior experience in fulfilling government contracts reported greater ease in obtaining details about new opportunities and meeting bidding prerequisites compared to first-time bidders. Accessing these contracts poses multiple challenges, including

difficulties in establishing relationships to assess competitive capabilities before bidding, fragmented and confusing information from different departments, limited comprehension of government decrees and regulations, time- and resource-intensive bidding processes involving multiple approval stages, negotiations, documentation, and waiting periods, constraints on pricing products and services (resulting in lower rates than those charged to non-government clients), restricted access to capital, and inconsistent demand from local authorities.

- There are multiple channels for searching information. The bidding process is transparent, so information is readily available and you can find it on any channel (respondent 8).
- Our company has fulfilled many contracts with state agencies, so we quickly received information about new contracts, and we meet the requirements pretty well (respondent 7).
- Through personal connections, we can learn information about our competitive capabilities when participating in the bidding process. Asking various departments is confusing, there are many decrees and regulations, and we don't grasp them all (respondent 19).
- The procedures are complex requiring bidding processes and multiple levels of approval, then negotiations, document preparation, and waiting, consuming a lot of time and manpower (respondent 6).
- Product and service prices are lower compared to non-government clients. We always have to quote lower prices (respondent 15).
- Limited capital policies have prevented us from taking on larger contracts (respondent 17).
- The demand for services isn't consistent; they only look for SMEs when needed (respondent 22).

Respondents noted that the detailed contract fulfillment process, complete with specific timelines provides clarity in execution. Moreover, requirements for work, products, services, and fulfillment conditions exhibit minimal annual variation, enabling SMEs with prior experience to manage subsequent contracts with relative ease. However, challenges persist, particularly regarding investment capital, delayed payments due to extensive documentation and procedural requirements, and shifting regulatory guidelines.

- The contracts are clear, with specific timelines, and the execution follows the stipulated process, making contract fulfillment smooth (respondent 26).
- The product is familiar and changes minimally. Overall, the process, conditions, and everything else are the same. There are adjustments, but not many. Therefore, from the second time we fulfill a contract, it's not too demanding in terms of the process (respondent 15).
- There are many procedures, involving multiple levels of approval, resulting in delays in acceptance and payment (Respondent 30).
- Many regulations and guidance documents are updated and changed frequently, leading to delays in finalization due to having to provide explanations and supplementary documents (respondent 27).

4.3.4. *SMEs' Aspirations for Accessing Government Contracts*

All 34 interviewees were SME owners or leaders with prior experience fulfilling government contracts. 30 interviewees expressed a desire to sustain partnerships with local authorities and government agencies through future contracts, viewing strong government relationships as conducive to business growth and a gateway to operational expansion. Conversely, 4 respondents were reluctant to pursue further government contracts, citing excessively low bids, capital tie-ups due to prolonged acceptance and payment delays, and overly complex payment processes.

- We maintain a good relationship with state agencies to facilitate other activities, connecting with more clients who are administrative agencies and many other clients (respondent 6).
- The procedures are excessive, acceptance and payment take very long, and so company capital is tied up. The bids are low while there are many incurred expenses (respondent 22).

4.4. Discussion of Interview Results

The interview results demonstrate that government connections significantly influence SMEs' innovative activities affecting all categories of innovation within these enterprises. Consequently, fostering opportunities for SMEs to engage in contracts with local authorities and government agencies can catalyze innovation.

Accessing and fulfilling government contracts are supported by the transparent and widely disseminated tender information available through multiple channels, ensuring accessibility for SMEs. Additionally, contracts are structured with clear procedures, timelines, and specific tasks, minimizing ambiguity during execution. SMEs face hurdles in navigating tender information, including inadequate understanding of regulations, decrees, and guidelines, inconsistent information from multiple departments, and uncertainty about competitive capabilities due to the time and resources required for bidding preparation. Additionally, bid prices are often lower than those offered to non-government clients posing a financial challenge that is exacerbated by capital limitations and delays in contract approval and payment restrictions from complex procedures. The majority aspire to maintain government partnerships, believing these connections unlock substantial growth opportunities.

5. CONCLUSION

The research results indicate that government relationships have the potential to foster innovation among SMEs in Vietnam. The authors propose the following recommendations for government agencies to maximize this potential and mitigate the challenges uncovered:

First, enhancing regulatory awareness, to mitigate the challenges faced by SMEs due to their limited comprehension of regulatory frameworks and constrained access to reliable bidding information, advisory teams should be established to provide consultation, address inquiries and guide bid preparation for SMEs. Regulatory updates should be disseminated through various communication channels and complemented by targeted training programs. Furthermore, fostering relationships with business associations could facilitate SMEs to exchange knowledge and experiences within networks.

Second, improving capital access, to solve capital shortages caused by SMEs' ability to pursue larger contracts or cope with payment delays, government agencies enhance SMEs' access to customized financial support mechanisms, such as investment funds, investor connections, and low-interest loans.

Third, streamlining procedures, to eliminate complex procedures and payment delays, government agencies should assign officials to support SMEs in the documentation process, ensuring payment processes align with fulfillment timelines. Government agencies should also clarify that these procedures help protect both parties' legal interests rather than being burdensome.

Fourth, highlighting long-term benefits, to clarify SME's concerns about low bids or payment delays, government agencies should explain SME's broader potential benefits, such as access to training on regulations and business skills, capital sources, partner networks, and promotional programs through seminars, conferences, and networking events.

In a nutshell, the above-mentioned four solutions aim to bolster SME innovation through government connections, and to offer practical guidance for SMEs seeking such contracts. However, this research has certain limitations. It focused only on SME managers in Hanoi, Da Nang, and Ho Chi Minh City, lacked comparative analysis across three cities due to sample distribution, did not categorize SMEs by industry, experience, or duration of government ties and mainly employed a qualitative approach. Future research could address these limitations by expanding geographic scope, comparing regional perspectives, classifying SMEs by key attributes, and adopting quantitative methods for broader validation.

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Transparency: The authors state that the manuscript is honest, truthful, and transparent, that no key aspects of the investigation have been omitted, and that any differences from the study as planned have been clarified. This study followed all writing ethics.

Competing Interests: The authors declare that they have no competing interests.

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