

**SWP 72/91 SMALL BUSINESS DEVELOPMENT IN THE  
DEVELOPING WORLD: AN OVERVIEW OF  
CONTEMPORARY ISSUES IN ENTERPRISE  
DEVELOPMENT**

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## **SMALL BUSINESS DEVELOPMENT IN THE DEVELOPING WORLD**

The recognition of the role of a viable small business sector in sustainable development has fuelled the debate as to the most effective and cost-efficient ways of promoting entrepreneurs and small-scale enterprises (SSE). The established pattern of supply side support for new and small businesses has been marked by heavy investment in the provision of key inputs - credit, training, advice, technical assistance and infrastructure. But increasingly questions are being asked as to the cost-efficiency of such measures and the efficacy of the institutions providing such services.

Research has not only highlighted the limited return on much of this support in terms of long-term growth, profits generated or jobs created; but has also stressed the importance of appropriate delivery systems and the institutional culture of enterprise support agencies. An increasing number of commentators suggest that it is the wider policy environment that is the key to whether any small business can survive profitably. Government policy, bureaucratic constraints and the politicisation of the enterprise development process have arguably had a greater influence on the viability of small businesses than any amount of finance, training or technical assistance provided by enterprise support agencies.

This paper attempts to review the small business sector in the development process, as well as provide an overview of contemporary issues in the promotion of SSE in developing countries, with particular emphasis on policy and institutional issues. The paper concludes by identifying some of the trends that may become apparent over the next decade in the promotion of the small business sector in the Third World.

### **SMALL-SCALE ENTERPRISE**

Efforts to define SSE have led to a remarkable diversity of definitions, and generated an unresolved debate as to the different approaches to defining SSE. Certainly anyone reviewing the current literature is struck by the diversity of terms used, let alone the range of definitions applied. Researchers, policy makers, and business advisers appear to use a range of terms interchangeably to describe SSE. These include microenterprise, the informal sector, small business, small firms, small enterprise, small-scale enterprise, small and medium sized enterprise, medium and small-scale industry, to name but a few.

An oft-quoted report noted that even in the mid-1970s seventy-five different countries had over fifty different formal definitions of SSE.<sup>1</sup> There is a strong body of opinion supporting this view that such diversity of definition is necessary and should be encouraged, if only because for a

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<sup>1</sup> K.E. Auciello, Employment Generation through Stimulation of Small Industries, an International Compilation of Small-Scale Industry Definitions, Atlanta, Georgia Institute of Technology, 1975.

definition to have any validity, it must be appropriate to the context to which it is applied. As Malcolm Harper points out,

the scale of a business needs only to be defined for a specific purpose, and there is no point in attempting to produce a universally or even nationally accepted standard. Any discussion of definitions should be preceded by a very clear understanding of the purpose for which the definition is to be used.<sup>2</sup>

This point of view was further articulated at the 1988 World Conference on Microenterprises in Developing Countries, a major forum for those working in the field of SSE promotion, where participants reacted to attempts to achieve a common definition by accepting that, because definitions of SSE varied from country to country, there could be no clear global definition.<sup>3</sup>

Yet, despite the difficulties in reaching a common definition for SSE, there is still some value in attempting to reach an agreed definition. Hertz argues that agreed international definitions are essential in order to promote multilateral understanding, share research findings, and promote economic co-operation.<sup>4</sup> Agreed national definitions are of value not only for research purposes, but also for reasons of consistency of legislation, and for focusing the discussions of policy makers as well as the work of banks and enterprise support agencies generally.

As a result there have been numerous attempts to define SSE, and these are usually based on either quantitative or qualitative characteristics. It is noteworthy that developing countries are more likely to apply quantitative definitions, and industrialized nations to apply qualitative measures.<sup>5</sup> In part this reflects the purpose for which such definitions are applied in developing countries, particularly their use in the development planning process. As Neck commented, "most definitions appear to be governed by the interests of the perceiver, the purpose of the definition, and the stage of development of the particular environment in which the definition is to be employed".<sup>6</sup>

### Qualitative Definitions

Qualitative definitions of SSE are inherently subjective, broad-based, and less precise than quantitative definitions. And although such definitions are of limited use in identifying eligibility for preferential treatment or for fiscal purposes, their value is that they offer conceptual flexibility and breadth of purpose. They commonly refer to operating styles, the degree of specialisation, overall aims and objectives, or the relationship with the local community and the wider commercial environment; for example in Tanzania small enterprises are those "within the reach of the people".<sup>7</sup>

Increasingly such qualitative definitions, with implicit societal connotations are gaining prominence. These are exemplified by the definitions of the micro-enterprises in the "informal

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2 M.H. Harper, Small Business in the Third World, Chichester, Wiley, 1984, p.2.

3 J. Levitsky, (ed.), Microenterprise In Developing Countries, London, Intermediate Publications, 1989, p.xx.

4 L. Hertz, In Search of a Small Business Definition, Washington, University Press of America, 1982, p.20.

5 M.H. Harper, op cit., p.2.

6 P. Neck, Small Enterprise Development: Policies and Programmes, Geneva, ILO, 1977, p.10.

7 M.H. Harper, op cit., p.5.

sector" which emphasise ease of entry, reliance on indigenous resources, family ownership, etc. Or the perceptions of practitioners like Mohammad Yunus founder of the Grameen Bank in Bangladesh, who sees little point in focusing on the characteristics or size of microenterprises, but prefers to dwell on their role in development which he suggests is to create employment, generate income and is so doing reduce poverty.<sup>8</sup>

### Quantitative Definitions

Quantitative definitions of SSE rely on clearly defined parameters, or combinations of parameters, which include one or more of the following: the number of employees, sales turnover, assets, capital, net worth, or even specific industry-wide measures (e.g number of fare paying passengers, number of hotel rooms, amount of energy consumed). In general quantitative measures are applied where it is necessary to clearly identify a specific target group and to exclude larger enterprises from preferential treatment. But quantitative definitions are marked by their range and diversity, and accordingly are of little use for purposes of international comparison.

The extent of the disparity between quantitative definitions is most clearly seen in the attempts to define a SSE by the size of its workforce. National definitions of SSE range from ventures which actually employ fewer than 10 employees (Western Samoa) to those employing fewer than 300 (Japan). But it is amongst those researching in this field that one can find the greatest disparity of definition. Thus d'Amboise and Muldowney can report that "for a growing number of researchers and reporting organizations, the small business is generally considered to employ no more than 500 persons and to have sales less than US\$20 million"<sup>9</sup>; whilst at the other end of the spectrum the 1988 World Conference on Microenterprise generally agreed that their target group comprised very small units possibly employing only one person or merely members of a family.<sup>10</sup>

Because of such definitional diversity, and the inherent constraints in both quantitative and qualitative approaches, there has been increasing acceptance of the limitations of definitions per se; particularly so when they are applied for reasons of international comparability. As a consequence, when definitions are used there is a tendency to merge quantitative measures with qualitative precepts. Such definitions often include operational characteristics, market share, turnover and number of employees.<sup>11</sup> In the light of this, and given the business conditions in many developing countries, SSE can be taken, for the purposes of this paper, to refer to:

"an independently owned and operated business that has a small share of the market and is personally managed by its owner, who employs five or fewer regularly paid employees".

8 Quoted in J. Levitsky, *op cit.*, p.xix.

9 G. d'Amboise & M. Muldowney, "Management Theory for Small Business", *Academy of Management Review*, 13(2), 1988, p.226.

10 J. Levitsky, *op cit.*, p.xx.

11 This is well exemplified by the definition finally applied in the 1988 World Conference on Microenterprise. J. Levitsky, *op cit.*, p.xx.

## THE ROLE OF SMALL-SCALE ENTERPRISE IN DEVELOPMENT

The growth of SSE is inextricably linked with the development process, if only because of the very high proportion of SSE found in developing economies. For example in Indonesia 99.55% of the manufacturing establishments are either small or handicraft industries, while even in a rapidly developing economy like Singapore, 97% of all businesses are SSE.<sup>12</sup>

The variety of different, but often essential, services that the small business sector provides also underlines its integral role in the economy of most developing countries. The extent of its contribution can be best assessed by identifying the range of services provided by SSEs; these include amongst others: bicycle repair, baking, blacksmithing, brickmaking, carpentry, carving, computer services, dry cleaning, electronics, furniture making, knitting, motor repairs, photography, pottery, retailing, shoe making, tailoring, transport and welding. It is obviously difficult to quantify accurately the impact of such a diversity of enterprise, especially as they are often best described in qualitative, ideological, or even emotive terms; but the evidence suggests that the small business sector does play a major role in the local economy.

The contribution of the small business sector to national development can also be assessed in terms of a range of inter-related economic, social and political issues. The economic contributions include employment creation, wealth creation, increased output, mobilization of local resources and adaptation of technologies. The social benefits include a reduction in poverty, balanced development, provision of goods and services appropriate to local needs, a seed bed for new initiatives, redistribution of both income and opportunity in the community in general, and a greater degree of personal involvement and commitment. The political benefits result from the redistribution of wealth, opportunity, and therefore power within the community.

### SSE and the Development Agenda

Partly for ideological reasons, and partly because of the emphasis on government-sponsored development and the associated preference for major industrial and infrastructural projects it took time for development strategists to recognize the contribution of small businesses in promoting balanced development. In the 1950s economists like Bert Hoselitz reviewing the relationship between entrepreneurs and economic growth attempted to establish entrepreneurship and small business on the development agenda.<sup>13</sup> Their work was followed in 1965 by the publication of Staley and Morse's classic study Modern Small Industries for Developing Countries. This research not only provided evidence supporting the role of small business in economic development, but also offered one of the first conceptual frameworks of the policies and institutional support necessary to promote a range of SSEs.

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12 T.T. Soon, "South East Asia", in D.J. Storey, (ed.), The Small Firm: An International Survey, London, Croom Helm, 1983, pp.218-247.

13 B.F. Hoselitz, "Entrepreneurship and Economic Growth", American Journal of Economics and Sociology, Vol.12(1), 1952, p.106.

In the 1970s the process of fixing entrepreneurship and small business on the development agenda gathered pace. In 1971 Peter Kilby's Entrepreneurship and Economic Development was published.<sup>14</sup> This much quoted collection of research studies highlighted the role of entrepreneurs and small businesses in the development process; as did Schumacher's Small is Beautiful, published in 1974. This book, not only captured the public's imagination, but helped to legitimize the work of those trying to promote sustainable small-scale enterprise. Schumacher argued that it was only in such businesses that "private ownership is natural, fruitful and just".<sup>15</sup>

Mainstream development thinkers were also beginning to recognize the potential role of such small-scale self-sustaining ventures. Dudley Seers, for example, had identified the five primary objectives of development as being: 1). to ensure adequate family income to provide subsistence essentials; 2). to create sufficient employment to allow for the continued redistribution of income and opportunity; 3). to increase access to education and improve literacy rates; 4). to enhance the ability of the population in general to participate in government; and 5). to promote national independence.<sup>16</sup> However, Seers later acknowledged that he had omitted a key ingredient from this analysis - the need for any individual to become self-reliant. As a consequence of which he began to emphasise the importance of "ownership as well as output" as an integral part of the development process.<sup>17</sup>

This belated recognition of the need to promote individual self-reliance, and individual ownership reflected a growing awareness in mainstream development thinking that individual entrepreneurs and small business sector in general was an integral part of the development process. This shift in thinking was given further impetus in the mid-1970s when researchers and policy makers acknowledged the significance of the informal sector. In many less developed countries the informal sector, which often encompassed the majority of the population, was the centre of entrepreneurial activity, and the SSEs common to this sector generated a significant proportion of national economic activity. This in turn further focused the attention of researchers and policy makers on the role of entrepreneurs and SSEs.

The 1970s and the 1980s were marked by growing economic instability, indebtedness and unemployment within the formal sector. Governments faced with such economic constraints had to reduce their role in the economy, adopt stringent readjustment policies, and turn to the private sector as a vehicle for growth. Aid agencies established small business programmes, and a new breed of specialist enterprise development professional was created.

It was therefore no coincidence that the small business sector became established on the development agenda. A state of affairs reinforced by the recognition of the contribution of the small business sector to wider socio-political development. Entrepreneurs and the small business community have been credited with playing a role in promoting Independence and generating a more egalitarian society marked by democratic political structures. It is argued that the dynamics of the small business community foster a climate of self-reliance, create new internally-derived opportunities and generate confidence in indigenous abilities. Marris and Somerset suggested that

14 P. Kilby, Entrepreneurship and Economic Development, New York, Free Press, 1971.

15 E.F. Schumacher, Small is Beautiful, London, Abacus, 1974, p.223.

16 D. Seers, "The meaning of development", in N. Bastor, (ed.), Measuring Development, London, Cass, 1972.

17 D. Seers, "The new meaning of development", International Development Review, No.3, 1977, p.5.

entrepreneurship was part of "the transfer of power for which Independence stands".<sup>18</sup> While Berkoff notes that:

"One indispensable condition of economic independence is the manpower which will initiate and uphold new and constantly increasing numbers of enterprises. Any country which aims to become self-supporting must have an adequate reservoir of men who have the judgement, the initiative, the courage and the determination to conceive and launch new enterprises".<sup>19</sup>

### Questioning the Role of SSEs

Despite the evidence as to the developmental role of the small business sector there was a contrary perspective which indicated that any investment in the small business sector could well be a misuse of resources. Research suggested that SSEs made little real contribution to growth, and instead merely generate unwanted surplus capacity which kept prices uneconomically low. Some policy makers still see SSEs, with their low level activities and the high failure rate as an obstacle to "modernization", because they waste resources and are a threat to economic rationalization. This argument is supported by concern at the number of small business failures, and the perception that investment should be directed instead to less risky large-scale operations that can contribute more effectively to national growth. Recent studies have also questioned the cost-efficiency and productivity of SSEs. Ian Little, for example, argues there is no consistent relationship between the size of firm, labour intensity, and capital productivity.

Little points to three inter-related pieces of evidence. First, SSEs produce a relatively small percentage of manufacturing output in countries, such as South Korea, which have high growth rates and clearly defined industrialization policies. Second, his evidence points to SSEs being less efficient users of capital and labour. Third, that it is questionable whether SSEs can actually create worthwhile cash employment, therefore reducing poverty and inequality, because the evidence suggests that SSEs are rarely able to increase output sufficiently to absorb new labour.<sup>20</sup>

Little's perceptions have provoked a detailed re-analysis of some of our basic assumptions about the role of SSE. But further analysis has suggested that many of the benefits attributed to SSEs are still valid; and that Little's evidence merely suggests that size is irrelevant, and that efficiency depends on the type of industry and the type of machinery used. Little's conclusions have also been questioned: first, because his evidence was only drawn from a limited sample of manufacturing ventures that employed less than fifty employees (hardly small) in only two countries (Columbia and India); second, because of his reliance on official statistics that fail to reflect the reality of the informal sector; and third, because he was only concerned with economic measures of efficiency, and did not concern himself with other indicators such as the appropriateness of the goods or services offered.<sup>21</sup>

18 P. Marris & A. Somers, African Businessman: A Study of Entrepreneurship and Development in Kenya, London, Routledge Kegan Paul, 1971, p.6.

19 B. Berkoff, "Foreword", to B. Dinwiddy, Promoting African Enterprise, London, Croom Helm, 1974, p.vii.

20 I.M.D. Little, op cit., pp.203-235.

21 I.M.D. Little, ibid., p.205.

In conclusion, despite recent critical reassessment, the bulk of the evidence suggests that the small business sector was an integral part of political and economic development. SSEs appear to provide new opportunities for both the individual and the community in general. A healthy, viable small business sector which creates new jobs, introduces new techniques, opens new markets, and provides goods and services appropriate to the local community is arguably a prerequisite for equitable growth and balanced development.

### SMALL BUSINESS PROGRAMMES AND ENTERPRISE SUPPORT AGENCIES

Faced with this conclusion the question that then needs to be asked is what is the most effective way to promote such businesses within the constraints commonly found in Third World economies? This is particularly pertinent today in light of the resources being invested by aid agencies and governments in enterprise development programmes, and the concerns about the cost-efficiency of the established pattern of "supply side" support which has dominated enterprise development for the last thirty years. "Supply side" measures which are channelled through a range of enterprise support agencies, credit schemes, marketing organizations and industrial estates are intended to: a). provide SSEs with easier access to finance, b). improve performance through training, advice or technical assistance or advice, and c). provide basic infrastructure.

This integrated approach to enterprise development was pioneered in India in the early 1950s, and the "Indian Model", as it is sometimes known, has been applied throughout the Third World and has been described as one of India's major exports.<sup>22</sup> The "Indian model" not only offers a variety of assistance to range of small businesses, but also provided protection for certain industries or groups of entrepreneurs. It should be distinguished from the "Japanese model", which was based on promoting sub-contracting links between large-scale industry and the small business sector. The success of the "Japanese model" is a result of Japan's strong industrial base and its particular socio-cultural environment. Few developing countries enjoy such advantages, and so the integrated "Indian model" has been widely adopted throughout the Third World.

Staley and Morse were early proponents of the need for such "supply side" support, and emphasised the need for integrated programmes which could channel a range of assistance to local entrepreneurs and small businesses. They argued that "the need for such advisory services stems basically from the small firm's lack of management specialization in an era when specialized knowledge and techniques underlie most industrial progress".<sup>23</sup> Phil Neck identified eight key areas where such support should be directed: finance, training, markets, access to raw materials, manpower, technology, assistance and community relations. He also argued that development planners should fully incorporate a comprehensive programme of support for small businesses into national plans, because in the past the small business sector had only "second-class status", and existing policies had "indisputably favoured big rather than small business".<sup>24</sup>

22 T.A. Timberg, "Small Enterprise Promotion in India", Small Enterprise Development, Vol.1(1), 1990, p.26.

23 E. Staley & R. Morse, "Developing Entrepreneurship: Elements for a Program". In P. Kilby, (ed.), op cit., 1971, p.366.

24 P. Neck, op cit., p.1.



### Critical Commentaries and the "Minimalist" Perspective

The initial intention was that the support provided would be both interactive and complementary, but in reality it became enmeshed in a range of different institutions and agencies established to administer the support provided or decide who needed preferential treatment. Their programmes were often run by people with little business experience, became hidebound by restrictive legislation, and were perceived to be inappropriate, inflexible, and overly bureaucratic. Researchers such as Kilby, Little or Sandesera have highlighted the limited return of this support in terms of long-term growth, profits generated, or jobs created. Apart from the concerns that these measures were neither effective or cost-efficient, they were criticised for creating an over-protected artificial environment for their clients. As a result there has for a number of years been well-founded misgivings at the ill-conceived nature of many of these programmes. As Bryce commented back in 1965 most SSE support was:

confused by sentimentalism and approached emotionally with little regard for the costs and benefits involved, small industry development can easily become a missionary movement which accomplishes little but which diverts scarce resources of development funds and people away from other activities which, in most situations, could produce more industrial growth.<sup>25</sup>

Ian Little adopts a similar stance after reviewing the long-term cost effectiveness of the Indian experience of reserving certain industries for specific social groups. He suggests these policies have tended to reduce competition, prevent organic growth, artificially skew the market and in so doing have created unreal price differentials. Little concluded that these policies were "romantic, rather than economic", and were not based on an objective assessment of costs involved.<sup>26</sup>

Furthermore, research findings from around the world support the contention that small businesses which have received support over a long period of time perform less well than firms which have had to survive with no support. Thus, for example, Sandesara's studies in India demonstrate that firms located in government-sponsored industrial estates performed less well than firms outside. Such non-assisted firms had higher rates of profitability, higher capital productivity and higher surplus per unit of capital.<sup>27</sup> Research by Peter Kilby in Kenya showed similar results, and that between 1974 and 1985 firms receiving technical assistance from the Kenya Industrial Estates programme grew at 1.4 percent per annum; while companies which received no such assistance grew at 9 percent per annum.<sup>28</sup> Kilby had earlier used cost-benefit analysis to evaluate eleven ILO/UNDP small scale industry technical assistance projects, and concluded that in only three of the projects did the benefits exceed the cost.<sup>29</sup>

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25 M.D. Bryce, Policies and Methods for Industrial Development, New York, McGraw-Hill, 1965, p.77.

26 I.M.D. Little, op cit., p.232.

27 J.C. Sandesara, "Institutional framework for promoting small-scale industries in India", Asian Development Review, Vol.6(2), 1988, pp.11-40.

28 P. Kilby, op cit., 1988, p.229.

29 P. Kilby. "Evaluating Technical Assistance, World Development, Vol 4(3), 1979.

Faced with this evidence the minimalist perspective has gained a degree of credence. Minimalists favour "programmes which operate in a narrow focus supplying credit and no other form of assistance".<sup>30</sup> They question the value of providing a training or technical assistance, and instead recommend that small business programmes should merely focus on providing what Kilby refers to as the single "missing ingredient" needed by the client. Evaluation studies have confirmed the efficacy of the "missing ingredient" notion, and pointed out that where intervention provided an integrated set of multiple ingredients, the results were largely failures.<sup>31</sup>

The minimalist perspective has also been championed by those who think that training and technical assistance is expensive to implement and does little to ensure profitability in practice. Judith Tendler, an early advocate of the minimalist credit programmes, points to the number of evaluation studies which have cast doubt on how much this assistance actually leads to increased income. Her evidence suggests that fully integrated programmes with their "higher unit costs of lending and greater demands for organizational sophistication" rarely succeed in meeting the needs of large numbers of clients.<sup>32</sup>

For similar reasons Malcolm Harper argues that training has a limited role to play in the microenterprise sector. In particular he singles out training intended to develop "entrepreneurial motivation or behaviour" as being the least valuable form of assistance. He bases this proposition on the perception that the informal sector is already dominated by successful microentrepreneurs, most of whom only need finance speedily delivered with "as few strings as possible".<sup>33</sup> Walter Elkan also points out that there is little evidence of any positive returns on small business training, suggesting that its existence is probably better explained by the fact that such training is "regarded as costless by governments", rather than because of any real demand or need for it.<sup>34</sup>

### Evaluating Successful Small Business Programmes

The minimalist perspective is not universally accepted, and critics of the approach argue strongly that credit alone without training and technical assistance is of limited value. Credit given without adequate training is likely to be misused with the consequent poor results and waste of resources. Furthermore, despite the critics, a remarkable range of agencies and support measures exist in the Third World to facilitate and promote small business and local industry. One response to the minimalist's concerns has been to attempt to improve the effectiveness of these institutions delivering technical assistance to SSEs by assessing the organizational characteristics and replicability of the more successful programmes.

One of the first major reviews of small business assistance programmes was the PISCES Studies published in 1981. The researchers found only one precept that was common to all successful programmes which was that all programmes should be "responsive to the plans and

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30 J. Levitsky, *op cit.*, p.xxviii.

31 C. Liedholm & D. Mead, Small Scale Industries in Developing Countries, Michigan, MSU, 1987, p.112

32 J. Tendler, "Whatever happened to poverty alleviation", in J. Levitsky, *op cit.*, p.37.

33 M.H. Harper, "Training and Technical Assistance for Microenterprise", in J. Levitsky, *op cit.*, p.181.

34 W. Elkan, "Policy for Small-Scale Industry: A Critique", Journal of International Development, Vol.1(2), 1989, p.245.

desires of those they serve and to the degree possible reflect the level of skills and knowledge that commonly exists in the community". When this precept was violated, the researchers found that costs per beneficiary increased, while the number of people who could be served decreases significantly.<sup>35</sup>

Later studies reflect similar findings. Harper identified four characteristics common to successful programmes: 1). none of the programmes was run by a government institution, 2). minimal use was made of "foreign" experts, and maximum use of local staff, 3). the programmes stayed small and resisted the temptation to grow larger, 4). the people who ran the programme shared many of the features of the entrepreneurs they were trying to help.<sup>36</sup> Manu and Gibb's study suggested that the most effective institutions were the ones "closest to SSEs with respect to people, structures and processes employed". Successful programmes maintained their operational independence, charged fees and relied on diversified sources of funding, had private sector conditions of service, a flat organization structure which allowed staff greater autonomy.<sup>37</sup>

Hailey and Westborg's study of NGOs involved in enterprise development demonstrated that while international NGOs adopted a more developmental community orientated perspective with mixed success, indigenous NGOs have developed their own "business orientated" culture which appears to be more appropriate to the needs of SSEs. This culture is marked by clients being selected on their business potential with preference being given to individualistic privately owned enterprises. No grants were given, loans were offered at market rates, and a tight repayment schedule was enforced.<sup>38</sup>

Other studies have reviewed the efficacy or replicability of different credit programmes. For example, Liedholm and Mead's evaluation of USAID sponsored credit programmes highlighted: 1). the importance of providing working capital not fixed capital, 2). the need for a locally-based decentralized loan granting structure, 3). realistic interest rates to cover transaction costs.<sup>39</sup> Maria Otero concluded her review of microenterprise credit schemes by suggesting that they can only be sustainable if three ingredients are present: 1). high volume of lending activity, 2). appropriate institutional capacity to maintain and expand the programme, and 3). sufficient repayment rates.<sup>40</sup>

A common theme running through all these studies is for these programmes to keep contact with their beneficiaries, and deal with them in a practical business-like way. Thus successful agencies are those that have become embedded in the community, decentralized their operations, employed local people, and adopted a financially sustainable "business oriented" culture. Yet for all the resources invested in these programmes and the research being undertaken it has become increasingly apparent that the wider policy environment holds the key to whether a small business can survive profitably. Government policy, bureaucratic constraints and the politicisation of the

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35 J. Ashe, etc. The PISCES Study, Washington D.C, USAID, 1981.

36 M.H. Harper, "Small scale enterprise development", Crown Agents Review, Vol.3, 1987, p.25.

37 A. Gibb & G. Manu, "The Design of Extension and Related Support Services for Small-Scale Enterprise Development", International Small Business Journal, Vol 8(3), 1990, p. 21.

38 J. Hailey & J. Westborg, A New Role for Development Agencies, NGOs and Enterprise Development, DSA Conference, Glasgow, 1990.

39 C. Liedholm & D. Mead, op cit., pp.103-109.

40 M. Otero, "Benefits, Costs, and Sustainability of Microenterprise Assistance Programs", in J. Levitsky, op cit., p.220.

enterprise development process have arguably had a greater influence on the viability of small businesses than any amount of finance, training or technical assistance provided by enterprise support agencies.

## POLITICS AND THE POLICY ENVIRONMENT

Thus, while questions are being asked about whether entrepreneurs themselves and the small business sector in general actually benefit from such interventionist measures, attention is turning to the removal of the policies that artificially skew demand and the external constraints that inhibit their freedom of operation. It is obviously imperative for most entrepreneurs to have the skills, resources and freedom to run their own businesses, but all these are meaningless unless there is a ready market for their goods and services. The absence or presence of this market is largely dependent on the economic policies and development strategies pursued by governments.

### The Market Environment

In an ideal world government support for SSEs would consist of: a). increasing aggregate demand, b). providing basic infrastructure (water, electricity, education and technical assistance), and c). reducing government-sponsored barriers and regulation. Of these the former is the most critical. Demand can be influenced by any number of policies intended to favour or protect particular sectors of the economy, or introduced to pursue the governments ideological bent. Thus we see the markets in which small businesses operate being skewed by fiscal policies or tariff protection intended to favour larger industries; or exchange control regulations which overvalues the local currency and inhibits local investment.

There is an increasingly vocal body of opinion which believes that these attempts to manipulate the economy should be discontinued and that market forces should be allowed to operate freely. As Marsden comments, it is significant that "where small-scale enterprises have flourished, it has been in those countries where governments have allowed markets to operate with a considerable degree of freedom".<sup>41</sup> While Hernando De Soto in his seminal study of the dynamics of the informal sector, The Other Path, highlighted the impact of the policy constraints imposed by the "mercantilist system" which still governs the working of many Third World markets.

This system which was the hallmark of the economies of seventeenth and eighteenth century Europe is, as the author argues, still being applied by many Third World governments. Mercantilism is defined as a "politically administered economy in which economic agents are subject to specific, detailed regulations", and results in entrepreneurs having to "spend an increasing proportion of their time politiking, complaining, flattering and negotiating" rather than being economically productive.<sup>42</sup> Mercantilist controls constrain growth and economic diversification.

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41 K. Marsden, "Creating the right environment for small firms", Economic Development and the Private Sector, Washington, World Bank, 1981, p.14.

42 H. De Soto, The Other Path, London, Tauris, 1989, p.209.

In particular they restrict the operation of the small business sector, while protecting the monopolistic market position of state-run industries, parastatals, and oligarchic business interests.

### Government Controls and Regulations

Apart from their role in limiting the market opportunities of SSEs by manipulating the economic environment, government policies are seen as one of the greatest single constraints faced by the small business community. The literature on SSEs is, almost without exception, critical of the attitude of governments and regulatory bodies. Governments appear ambivalent as to whether or not to promote SSE, and as Harper comments, "Governments often destroy enterprises with one hand while trying to assist them with the other".<sup>43</sup> While Bromley points to the "repression" of small enterprise by many Third World governments, in the form of official harassment and even persecution. For example, municipal authorities who treat street entrepreneurs as unwanted "hustlers" who block the traffic and disfigure the environment.<sup>44</sup>

Government policy is often seen as discriminating against the SSE sector, because the restrictive regulations and excessive controls it imposes inhibits local enterprise and jeopardize profitability. They do this by applying excessive bureaucratic red-tape and imposing restrictive controls. These restrictions include prohibitive licensing arrangements, price controls, the onerous conditions involved in getting planning permission or business licenses, the cost of delays caused by government red tape, and the cumbersome, often arbitrary, procedures in granting loans, incentives, or concessions. De Soto analyses the operation of the entrepreneurial informal sector in Peru, and describes the way entrepreneurs have circumnavigated the maze of bureaucratic controls imposed by local and central government. He graphically demonstrates the impact of such controls by the fact that it took 289 days to get all the necessary approval to establish a small garment factory.<sup>45</sup>

It is also clear that some governments attempt to repress the small business sector, and discriminate against individual enterprise by enforcing strict planning regulations and local by-laws, or merely by condoning police harassment of individual traders. The reasons for this persecution are complex and often depend on the local political climate. Individual entrepreneurs are in some countries seen by the elite as a threat to the status quo, in others they represent unwanted competition to established business interests.

### The Politicisation of Enterprise Development

The fact that enterprise development is part of the political agenda in many countries is something that has been virtually ignored by writers and researchers in this area. Yet for many entrepreneurs and business advisers the politicisation of enterprise development is a fact of life which has either curtailed their ambitions or provided unqualified support however viable their business. On one hand politicians for reasons of national self-sufficiency or ethnic aggrandizement

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43 M.H. Harper, "Small scale enterprise development", Crown Agents Review, Vol.3, 1987, p.23.

44 R. Bromley, "Small may not be beautiful", in R. Bromley, Planning for Small Enterprise in Third World Cities, Oxford, Pergamon, 1985, pp.328-331.

45 H. De Soto, op cit., p.134.

have invested huge sums in efforts to promote the indigenous small business sector. While on the other politicians keen to maintain the political status quo or protect vested interests have promoted policies that contained rather than developed SSEs.

For a variety of social and political reasons some governments actively discriminate in favour of certain groups within the population to encourage their involvement in the small business sector. Very often such discrimination is along racial or ethnic lines. Thus, in Malaysia, a comprehensive set of policies were introduced in the mid-1960s to promote the indigenous Malay (Bumiputera) in business, while in India and Kenya, for example, certain sectors are reserved for locally-owned businesses. In some cases these policies include active discrimination against other elements of the population (often migrant minority groups) which politicians are becoming too dominant at the expense of the indigenes. The most extreme example of such policies was the expulsion of the Asian community from Uganda in 1972.

The lack of indigenous participation in the economy, and the small business sector in particular becomes a source of increasing political tension. In Fiji, for example, one can trace a pattern of growing political agitation to allow Fijian commoners to participate in the burgeoning private sector. It can be found in the speeches of Apolosi Nawai attacking overseas business interests during the First World War, or Sakeasi Butadroka's criticism of the Indian business community in the mid-1970s. Certainly the evidence suggests that there was considerable grass-roots support for the military coups of 1987 from indigenous Fijians resentful at their lack of participation in all sectors of the economy, particularly their nonexistent presence in the small business sector.

Yet the explanation for this lack of Fijian participation in SSE suggests that it was in fact the Fijians own political leaders who acted to restrict the rise of the Fijian entrepreneur and the growth of an indigenous small business community. The Fijian chiefly elite had consistently adopted policies that contained any upswelling of unfettered indigenous entrepreneurial activity. This indigenous elite had actively condoned policies that encouraged non-Fijians to dominate the private sector, while enabling them to maintain political control and retain vestiges of their traditional power.<sup>46</sup> This example highlights the situation in many developing countries where the political elite are fearful that members of an underclass might gain sufficient economic clout through their involvement in the small business sector that they threaten their interests and the political status quo.

Obviously further research is needed into the increasing politicisation of the enterprise process, and the long-term implications of the political establishment's active discrimination against a dynamic small business sector. Studies by De Soto or Bromley have already revealed how the "establishment" has inspired a wide range of anti-small business measures to repress the small business sector and inhibit local microentrepreneurs. This research emphasises the need for enterprise development specialists to look beyond mere economic factors, and recognize the impact of wider political considerations on the success of attempts to promote entrepreneurs and the small business sector in general.

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46 J.M.Hailey, Indigenous Enterprise: Issues in the Promotion of Fijian Entrepreneurs, PhD Thesis, University of Queensland, 1990, Chap.12.

## CONCLUSION

This paper was written with the intention of providing an overview of contemporary thinking as to the role and development of the small business sector in the Third World. But it is clear from any review of the research and literature that there are still deep-rooted divisions amongst those working in the field of enterprise development.

Debate still rages as to how best to define a "small business", there is contradictory evidence as to the impact of SSEs on national development, questions continue to be asked as to how best to promote new and small enterprises, and there is uncertainty as to whether technical assistance and similar interventionist support is of any real value. Furthermore, there is a growing body of opinion that recommends that resources should no longer be invested in interventionist support, and should instead be used to alter the wider policy environment and influence attitudes. Politicians and policy makers would be lobbied to create a policy environment conducive to profitable small businesses, while training would be provided for bankers and government officials who deal with local entrepreneurs.

Faced with such a confused picture it appears foolhardy to predict the pattern of future developments in this field. Yet from a review of the literature and visiting small business programmes certain trends are already apparent which may influence the development of the small business sector in the 1990s. Small business programmes are increasingly being run by autonomous NGOs or specialist intermediary agencies. These are adopting a more responsive "business oriented" approach to client needs, and ensuring sustainability by diversifying their income base, charging fees and monitoring client performance more effectively. They are becoming more selective, targetting clearly defined groups and focusing on individuals (rather than groups) with long-term growth potential. Finally there is greater emphasis on providing information, developing networks, promoting links with larger firms, and effecting change by lobbying local policy makers.

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