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Microenterprises in the Informal Economy: Leave them of Support them?

Introduction

In most developing countries there is an increasing awareness of the vital functions of small and microenterprises in the urban and rural informal economy in terms of supply, employment creation and vocational and entrepreneurial training. The urban informal sector comprises three major subsectors: crafts and small industries, trade, and transport. With urban growth in both metropolitan and rural cities, there has been a major shift from traditional to modem craft occupations. More than 50 per cent of craft occupations are concentrated in three trades: tailoring (appr. 35%), carpentry (appr. 12%) and metal and motor vehicle crafts (appr. 10%). In Nigeria with its long-standing craft tradition, there are about 1 million craft enterprises with an average employment size of 2,8.

This study seeks to contribute to tile awareness of the significance of **metal and wood crafts** in socio-economic development. lt is a secondary analysis of an empirical study on craft enterprises in Nigeria's informal sector conducted by H.K. Anheier and H.D. Seibel with a grant from the German Research Council (DFG). The first part aims at providing a better understanding of the socio-demographic attributes of microentrepreneurs in Nigeria's secondary sector, their entrepreneurial history and associated start-up problems and last but not least of the characteristics of craft enterprises such as size, equipment and production, success, income or economic integration. One focal point of the study is the examination of environmental constraints and operational problems faced by crafts in Nigeria's informal sector.

The sample survey comprised 493 small and microenterprises with 1-15 employees, operating in different branches (wood and metal) and markets within the informal sector of two urban areas with distinct environments: Lagos, Nigeria's prime city, and Ibadan, a more traditional city in the rural hinterland. One of the central questions of the study is, whether there are any differences across the four environments respectively subsamples (Lagos wood, Lagos metal, Ibadan wood, Ibadan metal) in terms of business characteristics, production, size, business problems as well as entrepreneurial and behavioural characteristics.

Another focal point of the study concerns the question which business strategies craftsmen use to ease or solve business constraints such as lack of finance, sluggish demand or precarious supply conditions which characterize most urban economies in developing countries. Informal sector firms have often been characterized as more innovative, dynamic and adaptable when compared to larger firms in the formal sector. To scrutinize this assumption, business strategies were examined in terms of start-up problems, insufficient equipment, obstacles related to business expansion, lack of credit, increasing competition and sluggish demand, insufficient supply of business inputs such as machines, electricity, raw materials or fuel, business location and integration into interest associations such as craft unions. Do informal sector entrepreneurs pursue more passive and/or active strategies to cope with business environments characterized by uncertainty and extreme scarcity or are most of them unable to solve business constraints?

The findings are relevant to those who are concerned with the formulation of policies for the development and improvement of craft enterprises in the informal sector.

Small and Microenterprises as New Entrepreneurial Target Group

In the 1970s a new entrepreneurial target group has been identified in Third World countries: *small* and *microenterprises,* the majority of which located in the informal sector (Koll 1971; ILO 1972; Hart 1973; Sethuraman 1981). Major sectors where such establishments operate, include small industries, artisans and crafts, agricultural processing, trade, transportation, gastronomy, home and cottage industries, agriculture, fisheries and animal husbandry. About 75 per cent of Africa's labour force can be characterized as small or microentrepreneurs (peasants, craftsmen and traders). According to several data sources, the self-employed *craftsmen* respectively *small-scale industrialists* ratio in African countries is 1/58 inhabitants in urban regions and 1/174 inhabitants in rural areas. The World Bank estimates craft employment in tile informal sector in Nigeria to range between *2.5* and 5 Mio. or 85 per cent of overall industrial employment.

The new approach in development policy (‚small is beautiful') reflected the negative experiences of many Third World countries with Western models of modernization, capital-intensive industrialization and the failure of ‚trickle-down effects' and technological development. In view of rapid urbanization, increasing rural and urban poverty, high unemployment rates and expansion of spontaneous settlements (Gilbert 1982), it became obvious that something was wrong with the underlying hypotheses of Westernization and accelerated growth theories, according to which the expansion of the modem industrial sector would absorb many of the urban and rural surplus labour.

Research during the 1950s and 60s (Callaway 1965; Kilby 1963; Koll 1969; Lloyd 1953) failed to attract international attention and has remained inconsequential. Epoch-making, however, was Keith Hart's study on migrants in Accra (Ghana) and their various *informal income-generating activities.* Following Hart's approach, the missions organized by the International Labour Office/ILO (World Employment Programme) stressed that the promotion of informal sector activities would lead to a more equitable distribution of labour, incomes and resources, thereby mitigating social and spatial income disparities:

> ,,In many if not most developing countries, small or very small enterprises are the largest employers, providing a productive outlet for the entrepreneurial spirit of individuals and assisting in the dispersion of economic activity throughout the country" (ILO 1986:7).

The Heterogeneous Nature of the Informal Economy

The ILO country studies have documented the heterogeneous nature of the urban informal economy in Third-World countries and its different subsectors (often labelled as community of the poor, street economy, small-scale family enterprise sector, intermediate sector etc.) outside the ‚protected' formal sector enumerated by the government.

In its by now classical Kenya study the ILO (1972) tried to identify the informal sector against the formal sector according to economic criteria such as productivity, size, degree of organizational development, levels of incomes and profits, technology etc. According to the findings of the ILO, informal sector activities were characterized by (a) ease of entry; (b) reliance on indigenous resources; (c) family ownership of enterprises; (d) small scale operations; (e) labour-intensive and adapted technology; (f) skills acquired outside the formal school-system and (g) unregulated and competitive markets.

The report (ILO 1972:6) stressed that informal sector activities are largely ignored, rarely supported, often regulated and sometimes actively discouraged by the government. The characteristics of formal sector activities in contrast were characterized by: (a) difficult entry; (b) frequent reliance on overseas resources; (c) corporate ownership; (d) large scale of operations; (e) capital-intensive and often imported technology; (f) formally acquired styles, often expatriate; and (g) protected markets (through tariffs, quotas and trade licences).

If production units are not officially recognized, registered and safeguarded by law, they belong to the formal sector. If government subsidized credit sources or social security regulations are missing (Mazumdar 1976: 655ff), and if wages and conditions of work are not protected by trade unions or governments (Joshi/Lubell/Mouly 1976:49), they belong to the informal sector. The concrete measurement, however, remains vague due to its multifaceted structure:

> ,,The informal sector enterprise can be interpreted as belonging to the lower end of the urban continuum of enterprises... the term ‚small enterprise' is commonly and can be interpreted as belonging to the middle of this continuum; it uses the mode of production and Organisation somewhat similar to the formal sector enterprise but on a relatively smaller scale... Perhaps the distinguishing feature between the informal sector unit and the small enterprise is their orientation: whereas the former is motivated primarily by employment creation, the latter is concerned primarily with profit maximization" (Sethuraman 1981:13).

The following informal production units were distinguished: (a) production units consisting of a single individual without a fixed place of work and predominantly in petty trade and personal services; (b) family production units, small units which are primarily family enterprises including cantines, shops, etc.; (c) small and medium-size production units hiring several wage-workers, including garage workshops, small bakeries, barbershops, carpentry shops etc. (ILO 1978:33). Small and microenterprises with up to 10 employees are usually regarded as informal sector enterprises.

Among the ‚urban poor', ‚low-income households' and ‚urban population living in slums and squatter areas' (Sethuraman 1981:14) - which attracted the attention of the ILO and other institutions in the early 1970s - it is *the target group of the self-*

employed proprietors of ‚productive' small and microenterprises which are usually ignored and harassed by the government:

> ,,It consists of small-scale units engaged in the production and distribution of goods and services with the primary objective of generating employment and incomes to their participants notwithstanding the constraints of capital, both physical and human, and knowhow" (Sethuraman 1981:17).

Forms of dependent employment in the informal sector, including seasonal workers and day-labourers in the modern (formal) industrial sector who work below the minimum wage level, are largely neglected in the research promoted by the ILO.

Notwithstanding the theoretical debate on the informal sector concept and the wealth of critical essays (Märke 1986:64-106), the ILO has repeatedly emphasized that the bulk of employment in the informal sector is far from being only marginally productive but that it is economically efficient and profit-making. E.g., the informal sector often functions as a distribution channel for the formal sector. It contributes to economic growth through the purchase of raw materials, from the sale of finished products to the modern sector and through the training of skills that can be later used in the modern sector (Fapohundo/Lubell 1978:59,60).

The informal sector is seen as a production sector that buys inputs from the modem sector, uses its cheap labour to produce goods and services, and thus sells these cheaply to the modern sector:

> ,,Many motor mechanics who have worked for the big motor firms leave after a few years to establish their own business. This has succeeded so well that it is cheaper and faster to take some types of cars such as Peugeot and Volkswagen to these so-called road side mechanics instead of the dealers. In many cases, the quality of work is almost as good as that done in the firms' repair workshops. Another industry in which the informal sector has made inroads into the formal sector is the manufacture of furniture. High quality chairs and tables are being produced by carpenters in Lagos. Except for very high class cushioned living room sets, it is often cheaper to buy furniture in Lagos from the carpenters than from the formal sector" (Fapuhundo/Lubell 1978:59).

The development strategy of the International Labour Office is aimed at integrating a certain group of informal sector firms and actors (read the most dynamic production units) into the market system.

There is a lengthy debate in development literature on the meaning and usefulness of the *dualistic* informal sector concept (Jamann/Menkhoff 1988:51-70; Peattie 1987). In reality, there may be a closer articulation between the informal and formal sector than commonly realized. Attempts to draw an artificial border line between both alleged sectors perpetuate earlier dualistic conceptions and dichotomies such as those by Geertz (1963), McGee (1973) or Santos (1979).

ILO's approach that the relationship between the informal and formal sector is *benign* as well as its multiple policy recommendations to promote this sector and to strengthen intersectoral links (for example in the form of subcontracting etc.), have been criticized by several authors. It was argued that the relationship between the informal and formal sector is not characterized by an equally entitled exchange relation under normal market conditions but extreme dependence and exploitation at the expense of the informal sector. The production of cheap consumer goods by informal sector firms leads to a low subsistence level for the urban poor. This in turn enables formal enterprises to pay low wages and to avoid the provision of costly social benefits. The increasing *reserve army* of the informal sector in combination with low wages and long working hours thus facilitates formal sector firms' capital accumulation (Moser 1978: 1058ff).

The conclusion of these studies is that the promotion of small-scale enterprises enables a few small entrepreneurs in succeeding horizontal and vertical mobility (eventually obtaining formal sector status) whereas the majority of the urban population is exposed to increasing poverty and marginalization. It is beyond the scope of this study to discuss these conflicting ideas in greater detail which

> ,,...appear at the two extreme ends of the spectrum and ignore much of the diversity of activities in the middle ground, where no doubt most of the real world situations he" (House 1984:279).

This study starts from the assumption that craft enterprises in the informal sector and indigenous organizational structures such as self-help organizations deserve attention and perhaps active support due to their significance in socio-economic development. The development potential of indigenous economies is enormous yet far from being fully exhausted.

Entrepreneurial Bottlenecks in Africa

Since the early 1980s it has been repeatedly argued that small and microenterprises can provide a fertile soil for the formation of modern entrepreneurship in African countries. Whereas modernization theories started from the principle of a capitalistic, profit-oriented world, Africa's reality rather resembled a series of government programmes in form of Five-Year-Plans, supported by bi- and multilateral donors. The entrepreneur as central figure of the capitalist economy was replaced in Africa by planners and bureaucrats (Seibel/Anheier 1987:603). In many African countries the state became the most important entrepreneur as indicated by the large number of public corporations in which the government has controlling interests:

> ,,The dawn of development planning in Nigeria, which came at the end of the Second World War, involved the transformation of some utilities (water, railways, ports, and electricity which were previously under the civil service) into public corporations. Since then public enterprises grew phenomenally in both number and economic significance in the country. In respect of 31 of them that were named in the Fourth Development Plan
> the sum of Naira 22,7 Billion was earmarked for capital projects, representing about 54 per cent of the global provision budgeted under the plan. Today there are over 100 public enterprises at the federal level alone. The most familiar parastatals are utilities, but many of them are involved in the direct production of such commodities as steel, sugar, fertilizer, paper, textiles, and hotel services" (Ikpeze/Okorafor 1990:481).

Even in countries with liberal economic policies such as Togo, eleven of twelve large-scale enterprises belong to the state and the parastatal sector respectively.

Beside the strong influence of political elites and political entrepreneurs in Africa's economy and society, there are other factors which are responsible for the dearth of ,modern' African entrepreneurship and managerial competence:

- The cooperation between foreign capital, multinational corporations (MNCs) and African elites with their negative influence on indigenous entrepreneurs who play(ed) a subordinate role, overtaking the unproductive function of rentiers and compradores.
- The lack of a development ideology that would have been conducive to open up entrepreneurial potentials at the grassroot level.
- The sometimes restrictive influence of indigenous value systems, emphasizing group welfare, distribution and demonstrative consumption rather than the maximization of capital.
- The complicated agricultural property system with communal ownership of land (customary law) and the absence of individual property concepts (Seibel/Anheier 1987: 603,605).

The Development Potential of Small and Microenterprises

Small firms can play an important role in developing countries. Development strategies, stressing ,development from below' and self-sustained growth instead of large-scale industrialization based on foreign capital and technology inputs, are often based on small enterprises. Small enterprises help to satisfy basic needs. They can mobilize indigenous potentials by using local resources as inputs. Their surplus can be invested locally or regionally for the benefit of diversification and local customers.

Small businesses frequently occupy market niches which are unattractive for large corporations due to low profit margins. Small firms can strengthen domestic economic cycles and inter-sectoral relations, necessary preconditions for successful industrialization strategies. Another advantage, especially in countries with a large proportion of agriculturalists and underdeveloped industrial relations, is that they can utilize cheap, labour intensive and appropriate technologies. In geographical and spatial terms, small enterprises can have considerable radiation effects depending on their location (Vorlaufer 1988).

The mobilization of indigenous potentials by small firms can help to mitigate the dependence on external factors and the world-market system. It strengthens self-reliance and the development of local technology.

Local small-scale industries operate more economically with regard to the utilization of scarce resources such as capital than medium-sized or large-scale firms who largely rely on foreign markets. The internal market of many developing countries is limited during the initial stage of industrialization. In countries where the internal market is large enough for medium-sized and large-scale enterprises, small-scale firms can play an important role in the process of import-substitution, for example as suppliers of assembling industries or by overtaking ancillary works. For many medium-sized and large-scale enterprises, the existence of small-scale industries is an important precondition for their rentability. In case of repair or other unforeseeable problems, large-scale enterprises are reliant on lengthy imports and costly stocks, unless they have established subcontracting ties with small firms.

Equal Opportunities for the Informal and Formal Sector

However, the potential of indigenous or petty entrepreneurship is far from being fully developed. In most of Africa, economic policies implemented by civil or military regimes are not tailored for small and microenterprises. They are disadvantaged compared to large-scale corporations. Tax, customs and monetary policies often discriminate against smaller firms. Theoretically, economic, social and financial policies could compensate for such market distortions. In practice, however, the state often perpetuates the status quo and aggravates the problems of small enterprises concerning capital, raw material supply or demand (Williams/Tumusiime-Mulebile 1978).

The economic power of public and other large-scale enterprises and the dose connection of their representatives with political bodies contradict the neo-liberal ideal of ‚free competition'. In expectation of prestigeous management posts, high revenues and foreign exchange earnings, large-scale enterprises and multinationals receive preferential treatment by state bodies in terms of licenses, land concessions, tax holidays, favourable import/export regulations, customs policies, capital transfer and other incentives. But even a balanced combination of large-scale, medium-sized, small and microenterprises (Graf 1989:15) is no sufficient precondition for ‚take off'. Macroeconomic dynamics depend on multiple factors such as terms of trade, balance of payments, per capita income, debt service, GATT, political power etc.

Indigenous political and economic elites still treat small and microenterprises in the informal sector at best with ‚benign neglect'. They prefer prestigeous large-scale, capital-intensive development projects in spite of announcements to the contrary (Liedholm/Mead 1986:317). Nigeria is no exception. It remains to be seen how long public authorities can further ignore the rapid increase of informal entrepreneurial activities in urban regions, overlooking that this part of the economic sphere is no peripheral or transitional sector but a source for growth, employment and income generation.

How to Maximize the Development Potential of Informal Sector Firms?

Western donor countries and development agencies are convinced that the promotion of small industries in the informal sector has to be intensified. But the policy question remains, how best to maximize this development potential and, at the same time, to minimize the size of the community of the poor (House 1984:298; Fischer 1984; E+Z 5/1990:22).

In view of the increasing problem pressure in developing countries, there is the danger of overestimating the growth potential of informal sector enterprises such as craft workshops. SME and informal sector promotion programmes initiated and sponsored by ILO, World Bank or NGOs are not always successful. The behavioural rationality of craftsmen in informal sector economies is still little understood despite numerous studies. Many assistance programs ignore the opinions, interests, problems and needs of the respective target groups. A closer cooperation between donors, target groups, policy makers and researchers is necessary.

Problems of Small and Microenterprise Development

Among the major problems of small and microenterprises identified in the literature are:

- Inadequate policy framework for the small business sector
- Lack of support by indigenous policymakers and insufficient representation of the interests of the target group(s)
- Top-down planning
- Lack of support by the banking system
- Lacking efficiency of project holders
- Limited broad effects and sustainability of projects Limited markets

Measures to promote native crafts and to improve the self-help capacity of this sector should be based on existing indigenous organizational structures such as craft unions or self-help groups (Seibel/Damachi 1982; SeibeI/Holloh 1988: 161-170). Approaches such as action research, emphasizing the participation of those concerned in project and programme design (Gagel 1990), deserve further attention.

Urban and rural crafts in the informal sector as well as the entire small-scale industrial sector are very heterogenous in terms of productivity, entrepreneurial talents, profits, level of technology, capital assets, development prospects and so forth. They include tiny establishments with one worker, eventually operating dose to poverty line, small firms with up to 15 labourers and intermediate small-scale industries with up to 50. Some firms have succeeded in expanding and accumulating capital assets despite an often agressively negative attitude toward their activities by public authorities. Others are threatened by sluggish demand, rising cost and scarcity of raw materials.