

## Creating an enabling environment for private sector development in Sub-Saharan Africa

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### Executive Summary

This report discusses how the business environment in sub-Saharan Africa can be improved in order to foster enterprise development. Past efforts to boost private sector development have shown disappointing results. This holds especially for the orthodox structural adjustment programmes of the 1980s and 90s. But also the wide array of support schemes by governments and donors aimed to strengthen specific industries, groups of enterprises, or supporting institutions have rarely had a significant impact. Although a few remarkable project successes exist, these mostly remain isolated events with no country-wide outreach and no measurable effect on aggregate economic growth.

Against this background a new paradigm is now receiving considerable public attention. The World Bank/IFC has highlighted the importance of unnecessary government regulations as well as difficult access to property titles as some of the most important growth constraints, claiming that these reforms increase growth substantially and benefit the poor in particular. Since 2004 it publishes annual Doing Business reports providing detailed and comparable data on the administrative cost of doing business, thereby creating pressure on governments to spur property rights reforms and cut red tape. Donors are urged to help creating an undistorted “level playing field” for enterprises rather than providing support for specific industries or groups of enterprises. Other donors however continue to emphasize the relevance of support schemes to address specific constraints, e.g. to encourage entrepreneurship, foster business linkages, or enhance export competitiveness.

This study provides an analytical framework to compare the different approaches, making their underlying assumptions explicit and proposing a terminology to distinguish different notions of the ‘business enabling environment’. It shows that the Doing Business agenda is embedded in a neoclassical framework assuming that markets work reasonably well if property rights and competition are guaranteed. The agenda thus advocates minimal regulatory government intervention and a very limited role for supporting particular economic actors. Especially important for Sub-Saharan Africa, it presupposes a significant growth potential even for informal micro enterprises if unfair regulations are abolished. This is in marked contrast to neo-structuralist positions that emphasize market failure and the need for corrective policies, especially to enhance competitive advantages and to support disadvantaged groups.

Looked at from this perspective, it is important to identify the most important constraints for private sector development in Sub-Saharan Africa. This provides criteria to assess the effectiveness of alternative policy approaches. Although considerable variation exists across countries in Sub-Saharan Africa, the study makes out five distinctive structural deficits of the region’s enterprise structure that command the attention of policymakers: (1) widespread and rising informality; (2) a “missing middle” and lacking upward mobility of enterprises; (3) weak inter-firm linkages; (4) low levels of export competitiveness; and (5) lack of innovation capabilities.

From a policymakers’ or donors’ perspective it is thus imperative to learn which policies make African economies more productive and socially inclusive, in particular which ones

help to overcome the above deficits. The study examines the relevance and impact of three regulatory business reform areas that are emphasized in the Doing Business reports, namely easing business registration, providing property rights, and simplifying labour regulations. Preliminary findings show that reforms to ease business registration and the acquisition of licences seem to have the most favourable impact, saving businesses substantial amounts of money and time. However, there is no evidence that these reforms improve enterprise performance. Property titling programmes have not improved access to credit significantly. In some cases they have even resulted in anti-poor concentration processes. Simplification of labour regulations is partly necessary to spur labour mobility and increase wage flexibility. Again, however, there is little evidence to suggest that labour regulations are a significant growth constraint. Shortage of a skilled workforce seems to be a much greater limitation than inappropriate regulations. In sum, there is no evidence that the recommended reform packages are sufficient to unleash private sector dynamism. Most importantly, there is no evidence that policies aimed at establishing a “level playing field” are pro-poor and appropriate to lift the workforce in the informal economy out of poverty.

Instead, practical experience suggests a combined approach that builds on market forces wherever possible and offers targeted public support schemes where necessary. The study identifies measures to improve state-business relations, support innovative entrepreneurship, strengthen intra-firm specialization and linkages, promote exports and improve financial services as especially important to address the deficits of Africa’s private sector. Examples of successful, or at least promising, policy interventions from GTZ’s and UNIDO’s portfolios are provided. At the same time, the study stresses a number of principles of public service delivery that should be applied to avoid common errors of the past, e.g. the neglect of outreach and the distortion of existing service markets.