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

Tilman Altenburg / Christian von Drachenfels

5th November 2007
What are the challenges for private sector development in Sub-Saharan Africa?

- low productivity => low incomes
- widespread informality
- little upward mobility of small firms, a „missing middle“
- weak interfirm linkages, little specialization, short value chains, FDI/ large enterprises delinked from indigenous SMEs
- lack of innovation capabilities and export competitiveness ...

... **PSD reforms need to tackle these deficits**
Different concepts of „enabling environments“, different assumptions

**Neoclassical approach:** Assumes that most factor markets work reasonably well without government intervention if basic institutions are in place (property rights, competition, contract enforcement)

- **Narrow concept:** The ‘regulatory business environment’, focus on bureaucratic burdens and property rights problems (Doing Business indicators)

- **Broad concept:** ‘Investment climate‘ = RBE plus infrastructure, health, education, financial market etc.

**Neo-structuralist approach:** Assumes that market failure is pervasive and calls for more active public role, e.g. targeted enterprise support programmes
Neoclassical and neo-structuralist approaches
Different approaches to informality

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<th>Concept of informal economy</th>
<th>Neoclassical approach</th>
<th>Neo-structuralist approach</th>
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<td>Defined by lack of formal registration</td>
<td>Defined by multiple deficiencies (skills, capital, time constraints) and lack of absorptive capacity of modern economy</td>
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<td>Many vibrant opportunity entrepreneurs with viable business ideas.</td>
<td>Mostly necessity entrepreneurs with no long-term business plans, confined to simple activities with low entry barriers, oversupply and low returns. Run business to survive in absence of employment opportunities.</td>
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<th>Main policy implications</th>
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<td>Provide property rights, reduce bureaucratic entry cost and provide incentives for legalization.</td>
<td>Targeted policies for upgrading, e.g. providing management and technical training, support cooperatives, build linkages with formal enterprises, direct public purchases to informal sector organizations. Legalization may be helpful, but is not decisive.</td>
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How important is the regulatory business environment in SSA?

RBE approach highlights key role of:

- easing business registration and acquisition of licenses
- property titling
- simplification of labour regulations ...

... and questions need for / effectiveness of special public support programmes.

=> Empirical test for SSA:

1) Are RBE reforms successful?
2) Are special public support schemes succesful?
Are RBE reforms successful? Findings for SSA

1. Easing business registration / acquisition of licenses
   - saves businesses substantial amount of money and time
   - but no evidence of enterprise upgrading.

2. Property titling
   - encourages investment, makes transactions easier,
   - but has not significantly improved access to credit
   - and sometimes resulted in anti-poor concentration processes.
Are RBE reforms successful? Findings for SSA

3. Simplification of labour regulations

- evident cases of over-regulation (barriers to labour mobility, reduces wage flexibility) but
- few African enterprises perceive this as growth constraint
- no evidence that labour market flexibilization triggers employment and productivity growth
- Shortage of skilled labour more binding than over-regulation.

Summing up, reforms are positive, esp. deregulation of entry. But unlikely to remove most binding constraints. No evidence of significant upgrading & increased competitiveness. => Assumptions about growth potential of micro and small firms, „automatic“ increase of international competitiveness unrealistic.
Well known deficits (often bureaucratic delivery, low outreach, high costs, rent-seeking) ...

... but also some success stories (with limited outreach) in export promotion, entrepreneurship development, linkage building, MSTQ, etc.

⇒ combine investment climate reforms and special support programmes (e.g. liberalized FDI regimes plus incentives for supplier development)

⇒ apply strict principles to special support programmes.
Some principles for public support programmes

- Don’t just assume market failure – check whether market-based solutions may be viable
- Improve accountability of public agencies
- Separate funding from service delivery, measure performance, and link funding to performance
- Create competition among service providers
- Involve private sector in programme design and implementation
- make co-financing compulsory
- design upscaling / outreach strategies
- define exit strategy.