Title:
Three Perspectives for Improving the Business Environment: Towards a Systemic Approach. The Experience of FUNDES in Latin America

Author:
Elfid Torres G.

Date:
October 2005
Table of Contents

I. Executive summary 3
II. An Early Approach to Reform the Business Environment 5
III. Understanding the Latin American Business Environment 7
IV. Towards a Systemic Approach 15
V. Some Implications for Donor Agencies 20
References 24
I. Executive summary

Based upon the practice of FUNDES in Latin America\(^1\), this paper describes three perspectives to improve the business environment. Each of these views responds both to the needs or the features of different development stages of institutions in the region that are instrumental in the task of improving the business environment. Each perspective responds, also, to a better understanding of the SME sector and its exogenous problems.

Based on these considerations, the aim of the paper is to introduce recommendations that might be relevant for other organizations that, through the improvement of the business environment, strive to achieve SME development. Likewise, by encouraging the debate on the sufficiency of traditional approaches to improving business environment, it aims for a deeper perspective that we will refer to as “systemic”. With this in mind, each of the three lines of thought introduced here is treated from the point of view of their theoretical approach, their methods, tools and the actions implemented, as well as the sphere and actors upon which they operate.

The first approach rests on the thesis of institutional reform as logical frame for analysis and thought, taking the path of developing institutional agents in order to create a better business environment for SMEs. This approach made use of awareness tools to demonstrate the relevance of SMEs and the need for an institutional framework to promote their development. Since the issues and limitations to SME development identified by this means encompassed all of Latin America, the contents were generic, both in the subjects approached and in their geographical span.

---

\(^1\) In the mid-90s FUNDES established its Enabling Business Environment Program. The perspectives presented at this paper are derived from the practical experience of such Program in Latin America.
In this sense, this paper suggests that the usefulness of this approach decreases with the development of institutional frameworks for SME support in each country. Nevertheless, its transcendence should be acknowledged, since experiences with this approach have set the bases for other, more solid, mechanisms to deal with the reform of the business environment.

The second approach is based on a deep understanding —both qualitative and quantitative— of the SME phenomenon and the barriers that prevent their development. This approach, on the other hand, admits that, dealing with the business environment — according to the systemic competitiveness approach— requires actions at several levels (Esser, 1994). Advancing in the understanding of this principle is an important element in the development of this paper and the institutional experience it describes.

The third and last approach reflects deeply on the traditional points of view that deal with business environment and that, in general, concentrate their focus on the macro and the meso levels. This approach suggests the need to integrate the micro level into the lines that deal with the business environment for SMEs. A better understanding of SMEs and their issues has made clear that there are elements, exogenous to the firms, that are not related directly to issues belonging to the "public agenda", but, instead, to their interaction with other companies.

This paper also discusses the new theoretical approaches included in this third line of thought and compares it with the previous two in search of the differences they bear in terms of their scope, the elements of the business environment considered and the level of specialization required (see Table 1). Likewise, the paper emphasizes the complementarity of these three approaches, hence the relevance of putting forward a systemic approach to deal with the reform of the business environment that considers micro, meso, macro and even meta aspects.

The paper concludes by underlining some of the implications derived from the assumptions in the third perspective, in terms of donor agency work and, particularly, with regard to their approaches to dealing with the business environment, the elements that must be factored in, and the degree of specialization needed.
The thoughts expressed here leave the floor open for debate in terms of the mechanisms needed to deal with business environment reform from a systemic perspective. Some of these tools may be directly related with Business Development Services (BDS).

II. An Early Approach to Reform the Business Environment

Study and concern over the business environment emerged as a response to the evidence that traditional approaches of business development services—and financial services—albeit necessary, were not enough to guarantee SME development, since there is a host of other factors exogenous to their environment essential to their growth and, often, to their survival.

During the latter half of the 80’s, practical experience in Latin America had already evidenced the existence of elements over which the firms did not have a direct influence. There was not, however, an agenda based upon an inventory of these factors, or identifying their direct consequences on firm development, neither were there answers as to how to correct them or mitigate their impact. On the other hand, most of the countries in the region did not have a proper institutional framework to support SMEs, or agents with agendas oriented towards exerting direct influence on such elements.

In our days of global diffusion and specialization on the subject of the business environment, such scenarios seem unthinkable. Nevertheless, some countries found it necessary to approach the subject of dealing with the business environment, thus creating spaces where such issues could be debated.

Public debates—initially involving the participation of specialists and academic experts—on the situation of the environment and its impact on business development were significant in this sense. This experience was based upon the economic debates on the role of the State vs. the market, macroeconomic stabilization, structural adjustment, and, most of all, institutional reform emerging in the region since the late 80’s.

The first debates certainly yielded a series of generic analyses on political, institutional and legal conditions in several countries. They also created the conditions for opening
the debate to the participation of other actors with more incidence over the countries’
public agendas. In fact, one of the main purposes was to call the attention of decision
and policy makers on the need to set the bases for competitive markets, as well as to
raise awareness on the barriers that seemed to restrict business development at the
time.

Among other measures, the use of publications and events for lay audiences
summarizing such findings was intended to alert about the presence of barriers to entry
that prevented SMEs from participating in the formal economy, as well as on the
transaction costs firms had to face in order to remain in the formal market. These costs
were significantly high in certain countries, since their regulatory frameworks and the
charges imposed by their governments exceeded the profitability of most of the new
small firms (Sullivan, 1993). In this regard, it should be pointed out that, albeit the
progress evidenced in certain countries, this is not a settled subject in Latin America.

The very first path introduced some proposals for improving the business environment
favoring the institutional approaches. These proposals, however, outlined generic ideas
based upon standards and exclusions in terms of the size of the small enterprises

It is certain that there still remain elements that prevent business development in the
business environment of Latin America; but there are also many countries developing
institutional frameworks to mitigate these effects. Therefore, a strategy such as the one
described above might not be necessary anymore for certain Latin-American countries.
Nevertheless, this has certainly been a valuable experience from the point of view of the
work performed by donor agencies in countries whose institutional frameworks are less
developed.

On the other hand, such a strategy might contribute to establish the bases for
implementing other, more complete approaches to reforming the business environment,
and facilitates reaching the general agreement needed to implement public and private
initiatives that improve the business environment. The former applies particularly in
countries where the institutional framework and SME actors or agents are not sufficiently developed.

III. Understanding the Latin American Business Environment

Experience indicates that the above approach is useful to attract the interest of the relevant actors, thus contributing to the creation of an SME institutional framework. However, the very first debates on the problems and limitations faced by SMEs were plagued by a lack of understanding of the SME phenomenon as such. Today, we are aware that dimensioning the SME segment is instrumental as starting point of any analysis on the subject.

In this sense, the second approach is based upon two core elements that are also complements. The first factor would be the need of a deep knowledge of the SME phenomenon and the second is the admission that this is a systemic issue. Together, both factors have generated a series of mechanisms, implemented in Latin America, revealing the specific elements in need of change within the business environment.

In this particular instance, the study of the features that mark the SME segment came as a response to the need of building solid arguments to support the necessity for measures to improve their environment, not only in terms of its numeric relevance, but also of its economic and social significance. The study of this sector evidenced some typical SME weaknesses, such as low productivity, reduced or inexistent investment levels, and their short life or different levels of informality, among others. This only added to the generic diagnoses of the weaknesses in the institutional frameworks.

Numeric evidence usually intensifies the uncertainties regarding the specific causes that generate scenarios such as the high mortality rate of micro and SMEs or the relative decrease in the number of SMEs compared to that of micro firms.

This paved the way for more focused efforts, oriented towards raising awareness in political and entrepreneurial circles, in terms of the transcendence of SMEs in domestic economies, as well as of the relevance of its promotion by means of public policies, legislation and support programs. Later, in addition to the awareness-raising efforts,
these approaches required outlining a set of recommendations, even if only at the most general level.

The institutional reform arguments were brought back with this purpose, supplemented with the Systemic Competitiveness Approach, developed by the German Development Institute in the mid-90s (Esser, 1994).

*This concept seeks to capture both the political and economic determinants of a successful development process. The approach defines four key levels: a) the micro level, both for firms and firm networks; b) the meso level, that deals with specific policies and institutions; c) the macro level, regarding general economic conditions; and, d) the meta level, which concerns the slower variables, such as the socio-cultural structures, the basic order, the path the economy takes and the capacity of social actors to design strategies (Meyer-Stamer, 2000).*

The first approach is improved in the sense that, in this perspective, the situation of the business environment was no longer generalized for the whole region, but began to focus on more specific problems at the national level. Thus, starting with Mexico, a preliminary catalogue of the restrictions against SME development was outlined, based on the contribution of the dialogue with public, private and intermediate agency actors as well as with academic experts. The effort resulted in a first consensus on six general subjects: labor and fiscal reform, overregulation, access to financing, absence of SME-specific policies and, lastly, property rights.

This consensus paved the way for new awareness-raising actions among the relevant actors, in terms of the specific features of each of the six subjects. Discussion forums were organized on some of the topics, and international experts were invited to share their experience in the field of public policy, SME legislation and entrepreneurial promotion programs (Torres, 2002; Zevallos, 2001; Equihua, 1999).

Moreover, the systemic approach to competitiveness is quite suitable for this perspective, since it allows a clear identification of the requirements detected in the institutional reform analysis. For this reason, many of the awareness efforts directed towards decision-makers (such as forums, conferences, analysis and publications)
concentrated on the meso level, given that the approach evidenced that progress in the macroeconomic adjustment and stabilization reforms (macro level), albeit necessary, was not enough. Thus, for example, a lobbying agenda was ordered for Mexico with the purpose of positioning these subjects into decision-making levels where orthodox approaches dominated (the orthodox approach considers meso policies unnecessary, i.e., policies or institutions aimed at establishing industries at the local and national level). At the macro level, on the other hand, the agenda also emphasized the need to guarantee legal and political stability, since it is usual for macroeconomic issues to absorb most of the attention.

At some point in time, when contributions were exhausted at the discourse level, the need arose to go beyond the general description of the institutional issues identified in most Latin-American countries (Howald, 2001). Although the theoretical bases for the reform of the business environment—which had strongly depended on the institutional reform—still prevailed, a more pragmatic approach was followed in search of concrete proposals regarding the business environment problems previously identified. These proposals relied upon a diagnosis of the business environment conditions in the countries.

The first of these projects was implemented in Colombia, as a pilot program. The report (Howald, 2001) identified 34 different barriers to SME development imposed by the State, classifying them into 11 typologies (registration, labor-related, tax-related, financial, trade-related, infrastructure, social, legal, political, cultural and other obstacles). Likewise, the report stated the relationship among them and, more concretely, the weight of the tax system in this web of issues. The relevance of the tax system among the 34 barriers was determined based on a prioritization exercise that considered the opinions of entrepreneurs, intermediate agencies, and the State itself. Having identified the relevance of the tax system, the study then centered on the legal framework in force for the SME tax regime. In addition, with the purpose of determining entrepreneur perception of the tax system, a series of qualitative interviews were carried out. The study also compared tax legislation and practice, and analyzed the international
experience on this subject. The report concluded with a specific recommendation for small-firm tax supervision in Colombia.

This first experience established a model consisting of three core moments: first, the general diagnosis of State-imposed barriers SMEs had to face for their development in Colombia; second, analyzing the tax system, one of the most relevant problem areas for SMEs\(^2\); and, third, developing a concrete proposal to improve the SME tax regime.

The model established the foundations for a methodology under the following directives:

- Carrying out country-level studies
- *Action-oriented* research
- Including the *relevant actors* in the research
- Identifying *specific* issues
- Developing *concrete* solutions
- Give considerable weight to the *political* aspects
- Give significant relevance to *pragmatism*
- Implement recommendations and *materialize* concrete changes

By the same token, the approach sought to achieve real changes with measurable impact. To this regard, the premises were the following:

- *The lack of adequate conditions in the business environment seriously limits business development, particularly in developing countries;*

- *Unfavorable conditions in the legal and institutional frameworks damage SMEs, since this segment is particularly dependent upon adequate, stable and favorable conditions.*

---

\(^2\) Based, in turn, on four elements: 1) Analysis of the tax legislation; 2) Presenting the tax system from an SME point of view; 3) Comparing tax law and tax practice; and 4) Studying the knowledge achieved regarding fiscal theory and international knowledge of SME taxation regimes (Howald, 2001).
SMEs in Latin-American countries are not always thought of as strategic agents in the development of a competitive socio-economic system (FUNDES, 2002).

A definition was also adopted for the “Business Environment” concept: …every element surrounding the firm with a positive or negative impact on its performance that is out of its immediate control. From this particular point of view, the term might also include factors and circumstances beyond the scope traditionally attributed to the State.

Two basic concepts were identified for methodological purposes: The “barriers” beyond entrepreneur control and the “challenges” that lead entrepreneurs to develop new competences in order to guarantee their sustainable development and the State to design policies to support entrepreneurs during this process (FUNDES, 2002).

Again, the arguments that justified the need to quicken the pace to deal with the business environment materialized in the changes carried out during the 80s, when structural reforms began to be implemented and globalization efforts in the region accelerated. Such changes also modified the interaction among economic agents.

---

3 The term “barrier” is generally understood as the set of issues that damage SMEs in their different stages (startup, development or diversification theses) all sorts of restrictions that, due to market or State failures, damage or discriminate SMEs in their compliance with State requirements or that, as a result of the presence of barriers to entry, prevent access to certain markets instrumental for their expansion and survival. For a factor to qualify as “barrier” in the sense of the Program, it must have the following features: (i) Be perceived negatively by SMEs; (ii) Generate extra costs (in time and money); and (iii) Be beyond the control of the firm (“exogenous issue”) (FUNDES, 2002).

4 Structural reforms carried out in Latin America during the previous two decades, trade liberalization, financial liberalization and privatizations have radically altered the rules of the game that apply both to business and labor. As a result of these reforms, SMEs have experienced significant changes in their competitiveness conditions, even leading some of them to abandon their markets. It may be concluded, then, that the structural reforms carried out within the previous two decades have changed the business environment, particularly affecting SME performance. These firms have found it difficult to adapt to a new scheme that includes participation from large domestic conglomerates or local branches of transnational companies.

In the long term, the presence of a large and productive segment of small firms contributing to the systemic competitiveness of Latin-American economies, requires that SMEs adapt to such new context and develop new competences. A prerequisite for SMEs to be up to these challenges is the elimination of institutional and legal barriers, the establishment of stable rules of the game and a more balanced market access. However, it is equally important that SMEs improve their endogenous efficiency and create new ways to articulate with their environment, either with other firms or with the public or private entities with which they relate (FUNDES, 2002).
Since then, certain voices estimated that competitiveness requirements from the firms should be limited to macroeconomic stability —expected as a result of the adjustment programs implemented in the region— on one hand, and to developing abilities to adapt to this new context. Moreover, such abilities should derive from each firm’s initiative. Evidently, there was a need to determine the implications of the business environment on firm development and competitiveness, but this was a subject that had not been dealt with sufficiently.

With these considerations in mind, the pilot experience in Colombia and other early initiatives, an approach was established to deal with the business environment and strengthen SME competitiveness. This approach focused on identifying the main barriers to entrepreneurial development and designed solutions through consensus and technical foundations. The methodology designed and applied⁵ for these purposes consists of three stages:

- Stage I. – Diagnosis of the barriers in the business environment
- Stage II.- Developing Solutions
- Stage III.- Implementing Solutions

With the purpose of reducing the multiple dimensions of the regional situation and being able to make some interpretations⁶, the following general typology has been developed based on the outcome of eight diagnoses (Stage I) (Zevallos, 2005).

1. Finances
2. Infrastructure (and public services)
3. Macroeconomic policy and management
4. Labor and tax issues

---

⁵ This methodology has been implemented in eight Latin American countries: Argentina, Bolivia, Chile, Colombia, Costa Rica, El Salvador, Panama and Venezuela.

⁶ Results in each country are more detailed. For example, Chile’s survey (Bravo et. al. 2002), revealed that the most important barrier was in the conditions for competition, with the following elements as accompanying factors according to their relevance: prices under costs in large firms; non-compliance with regulations; informal producers; lack of fiscal supervision; subsidiary imports; smuggling; lack of information; and illegal copying of licenses and permits.
5. State operation

6. Analysis of promotion policies/actions

7. Social (and cultural) issues

8. Domestic market

9. International trade

10. Technology and innovation

11. Environmental issues

The multi-dimensional relationship between the State and the firms is among the findings of the eight diagnoses, in which the State plays the following roles: (i) providing a stable and investment-promoting macroeconomic climate; (ii) guaranteeing legal certainty and compliance with regulations; (iii) promoting public policies and actions in search of the common good; and (iv) collecting resources to carry out the above tasks. As part of each of these aspects, firms receive services, comply with rules and deliver resources, thus taking in both the weaknesses and the strengths of the government. (…)

Therefore, the key challenge for the region lies in developing policies that are the outcome of coordinated actions, establish agreed definitions and define the roles that each economic actor must play in development (Zevallos, 2005).

As it has been pointed out above, this approach and its methodology assume a complete process that, in addition to diagnosis, seeks to produce recommendations for concrete solutions and, eventually, for implementing such solutions. This is a permanent process, since the diagnosis identifies a set of problems that generate a series of recommendations for solving them, which, in turn, implies long-term efforts. In any case, the most valuable feature in this process is that the subsequent stages also involve decision-maker initiative.7

---

7 Examples of Stage II and III implementation may be found in Bolivia, Costa Rica, Chile and Panama, where programs have been implemented to solve issues identified through diagnoses, such as One-Stop Shops for Formalities, the Internal Revenue Service and the SME Promotion Law.
Awareness at public decision-making levels and the classification of entrepreneurial demands, useful for the lobbying agendas of intermediate agencies and entrepreneurial associations, are among the outcomes that emerge from this approach. This is particularly relevant in view of the lack of partners in SME-related dialogue. In fact, contrary to what happens with large firms, SMEs do not have the capacity to establish a dialogue with decision and policy makers, either because they lack organization or due to the absence of technical elements to support their demands with regard to policy, legislation or regulations impacting SMEs. This is a common situation in domestic environments, but it is identically relevant in the international sphere. This is evident, for instance, during free trade agreement negotiations where SMEs are usually underrepresented, albeit the fact that such agreements tend to affect them the most.

In this sense, key elements such as data processing and systematization and gathering opinions and defining needs by means of the mechanisms described above (forums, surveys, analysis) contribute in dealing with the reform of business environment when SME-related private institutions are absent or weak.

On the other hand, the diagnoses of the business environment usually bring forth government and legislator responses and are a valuable input in the creation of institutional frameworks, laws and public policies regarding SMEs. This is, clearly, an aspect where intervention from donor agencies might have a positive impact on board firm segments.

Until now, however, the approach shares certain similarities with those applied by other organizations that strive for improved business environments. As it has been made evident above, all of them are marked by a theoretical framework, strongly sustained on institutional reform, in which the State emerges as the main entity responsible both for the barriers and for the creation of an improved business environment.
IV. Towards a Systemic Approach

Diagnosing the nature of the barriers to SME development, and the methodology to achieve it, results in a snapshot of the business environment conditions in different countries, which is supported by a ranking of the issues that, essentially, indicate the starting point for public action. In fact, the two approaches introduced at this point evidence the prevalence of the State, in general terms, and of the institutional framework in particular, as the key elements that influence the identification of the barriers to SME development and, thus, to the construction of enabling business environments.

This is justified by the fact that the initiatives introduced until now had the institutional reform principles as logical framework, hence the domination in the business environment interpretation of subjects that we will define here as belonging to the “public agenda”, since their solving depends almost entirely on the State’s actions and that are usually represented by the barriers mentioned in the previous section. Up to this point, the approach matches the elements describing specific components of the business environment from the point of view of the donor agencies, as identified by White (2004): governance issues, policy framework, legal and regulatory framework and organizational framework, among others.

Moreover, even if the systemic competitiveness approach was incorporated as supplementary analysis framework, the approach introduced in the previous section continued emphasizing the weaknesses at the meso level. This situation is also justified by the fact that, in the early 90s, public attention was still focused on the structural adjustment programs, which, evidently, privileged macro action often at the expense or purposefully ignoring the meso level.

Meso level weaknesses were considered so serious, particularly in view of the experience in other regions (such as North America, Europe and East Asia), that the efforts to modify the business environment were directed to identifying the barriers at that level. The outcome of the diagnosis performed at these countries reinforced this view, perhaps because the theoretical frameworks sought, primarily, “the barriers imposed by the State”.
Although the relevance of the “public agenda” items is not discussed in terms of SME development, it is possible that the theoretical framework did not grasp the full dimension of other, equally relevant, issues. Concretely, this concerns certain elements from the micro level and other dimensions within the meso level that were not considered as relevant at that time. Similarly, certain factors that restrict or promote improved business environments in the meta level have not been analyzed in depth.

Again, when we further the study of the SME segment and the elements that restrict its development, we reach a third approach for improve the business environment, one that suggests that SMEs are influenced (positively or negatively) by other exogenous factors that are equally determining of, but unrelated to, the “public agenda”\(^8\). In fact, as attention turned to the meso level —for the reasons explained above—, micro considerations —which do take the systemic approach to competitiveness into account— were neglected\(^9\). Therefore, business environments, may also be approached from “micro” or even “meta” environments, in addition to “macro” or “meso” environments. Nevertheless, this paper focuses on dealing with the micro level as an enhancement of the approaches employed in the past.

In this sense, it is worth underlining that micro level interpretations have focused on operational efficiency issues in the firm, and that BDSs already act at that level developing certain abilities by means of training and advisory services. However, a key element at the micro level has been neglected: efficient firm networks (collective efficiency). Moreover, a subject that has lacked deeper analysis in the interpretations at the meso level is the contribution of private and intermediate institutions —which improve the way firms enter factor and product markets—.

These factors evidently affect firm performance, but their correction is also beyond their reach. The implications of the third approach also assume needs to modify or improve

\(^8\) Certain diagnoses already described part of this reality, specially in countries with relatively higher development levels (such as Chile) where issues related with market operation tended to emerge (e.g. competition conditions, export markets and supplier-distributor relationships) (Bravo et al. 2002).
firms’ micro-environments. With this in mind, this paper suggests redimensioning the micro level in order to expand its scope, so as to deal with the reform of the business environment by donor agencies.

The possible mechanisms for acting upon such micro-environments will surely generate new debates, since not only do they introduce a more holistic approach for dealing with business environment reform, but the methods employed in the first approximations of this approach differ from those described until now, as well as from those traditionally applied in donor agency interventions to reform the business environment. Indeed, the methods suggested approach the business environment to certain types of BDSs. It is worth mention that interlocutors also change under this perspective. Traditionally they are policy makers, but this approach needs to involve entrepreneurs both from SME and large enterprises (as in the case of Development Suppliers and Distributors Programs).

Based on these assumptions, a number of projects have begun to emerge at the practical level, focusing on both the micro and the meso sphere. This is particularly the case of ventures that have taken advantage of the accumulation of knowledge regarding the business environment and firm features, in order to develop sectoral or multi-sectoral initiatives that have resulted in productive and/or associative projects, in the design of private meso-level institutions or in business environment studies for specific sectors or regions. For each of these projects, the public agenda is not the sole factor—or the prevailing element—any more, although it still has considerable relevance.

The following examples illustrate this point more clearly.

A. Competitiveness Analysis
The number of barriers to SME development identified in the diagnosis contemplates the general situation of a country. However, there are also other important barriers in the business environment of the firm that relate to local or sectoral or multi-sectoral considerations. In this sense, the systemic approach has allowed the development of

---

9 It is also true that the systemic approach to competitiveness has gained from contributions and interpretations following its development. In fact, new related applications and methodologies have emerged (Meyer-Stamer, 2000); (Altenburg et al. 1998, 1999)
methodologies to identify the barriers that hinder or threaten the survival of specific sectors or regions. These procedures combine tools that may be related mainly to the BDS segment with others commonly employed for sectoral analysis.

With the aid of practical evidence on the subject, research projects have sought to determine the reasons of the loss of competitiveness\textsuperscript{10} in specific sectors. In any case, the analysis always assumes the reasons might be endogenous\textsuperscript{11} or exogenous. Particularly with regard to the latter, the focus is to identify if they concern the global, domestic or local environment. With this in mind, sectoral analyses have covered both the qualitative and the quantitative spheres. By the same token, the value chain has been analyzed with the aid of different tools, including the Porter analysis on market forces.

To illustrate the above, it might be useful to quote the case of a group of small banana producers in Southeast Mexico, for whom the barriers in their environment concerned the international regulations imposed by the European Union for banana trade (macro level). The latest trends in food distribution favoring large supermarket chains contributed as a factor of the business environment at the global and domestic level, also exerting a negative influence on its distribution (micro level). At the local level, the lack of backward and forward articulation in the value chain implied that local producers were at a disadvantage with regard to those of other countries who established strategic, long-term relationships with their suppliers and distributors (micro level).

The number of issues that threatening this particular sector did not minimize the relevance of other, more traditional, elements of the business environment, such as excessive regulation, the impact of fiscal policies, the absence of financing sources or the behavior of the State. They did, however, attract attention upon more specific agendas, whose treatment had a more visible impact and were susceptible of

\textsuperscript{10} Evidenced mainly by market loss or shifts by other agents belonging to the same sector but from other regions or, alternatively, by substitute goods.

\textsuperscript{11} The methods for determining the endogenous causes have to do with diagnoses assessing the operational efficiency of firms. Since their nature is directly related to the so-called BDS, they will not be dealt with in this paper.
intervention in the short-term, not to mention that the actors involved also react in private spheres, specially upon the micro-level factors.

B. Development of Competitive Advantages at Value Chain Level

Another experience in this sense assumed that competitiveness in the firm depends on its potential for innovation, which, in turn, is determined by micro-, meso-, macro- and meta-economic elements. Research on this subject sought to demonstrate that a firm’s performance in terms of the innovations achieved\(^{12}\) depends on three elements: i) the firm’s individual features, specially regarding its endogenous competences; ii) the firm’s relationship with suppliers and customers, with other firms (horizontally), and with the institutions in its environment (“productive” environment); and iii) the impact of the barriers in its business environment (non-productive environment).

The findings in the econometric study of a steel mill in Argentina confirmed the theoretical assumptions stating that competitive advantage is not a process that emerges automatically from the presence of certain exogenous elements (such as macroeconomic and institutional stability, market access and minimal discriminating interventions), but that is closely related to micro-, meso- and meta-economic-level factors (Schneuwly, 2004).

The findings underline also that a firm’s potential for innovation depends on endogenous factors, but advise that the achievements in this field are not a consequence of individual efforts, but of collective action.

It might be possible for the above approximations to generate new methodological approaches that reform the business environment from a systemic perspective that considers micro, meso, macro and meta elements.

Such approximations expose stages that have not yet been considered by more traditional approaches to the business environment. For instance, even at the macro and meso levels, they show that the ability to improve the business environment has

---

\(^{12}\) This paper adopted a broad and systemic concept of innovation that encompasses every successful effort made by a firm to maintain or improve its competitive stance. This includes: i) innovations in the goods or services that are part of this effort; ii) improvements in productive processes or in task organization; and iii) innovations in product marketing (Schneuwly, 2004).
exceeded the capacity of national States, since decisions in some fields concern supranational entities or are made simply in terms of market response and reorganization. On the other hand, the business environment is also influenced by elements that might be defined as “productive”\(^{13}\).

From this perspective, how can the “public agenda” create a better business environment all by itself when faced with conditions beyond its reach? Who are the actors that have to be influenced and made conscious in these scenarios?

A number of the answers attempted have to do with expanding the scope of action of the approaches seeking to improve the business environment. This should not suggest a change of approach, since it is clear that the institutional framework in Latin America is an unsolved area, albeit the significant progress observed in certain countries. On the contrary, this debate intends to complete the approach based on institutional reform and the meso level of the systemic perspective by expanding it with the inclusion of additional elements at the micro level that have not been sufficiently treated in the past.

Although this paper makes suggestions mainly at the micro level, the approach should extend towards the meta level, that includes measures for progress, for instance, by promoting entrepreneurship among larger population segments. This, without a doubt, is a sphere of action for donor agencies.

V. Some Implications for Donor Agencies

The two approaches described in previous sections (which essentially apply the principles of institutional reform) reveal significant similarities with the perspectives for improving business environment identified by White (2004) in the work of donor agencies. Such work evidences a relative agreement upon the approaches and methods employed to deal with this issue.

\(^{13}\) Schnewly (2004) employs the degree of linkage among firms to describe such productive environments, distinguishing between i) the degree of commercial linkage between a firm and its main customers; and ii) their degree of interaction with the agents that constitute their productive environment.
This paper seeks to compare the elements in both approaches, their theoretical bases, their objectives, tools, actions and sphere of influence with those of the last approach, which proposes the incorporation of micro-level elements (see Table 1).

In this sense, this work intends to attract attention particularly with regard to the adequacy of the approaches based only upon institutional reforms, which result in concerns that relate to what we define here as the “public agenda”. This is part of the elements considered when assessing the business environment and, thus, the definitions of interventions from donor agencies.

In this sense, one recommendation would focus on completing these approaches with micro-level factors, such as the relationship of the firms with their productive environments, i.e., their contact with other firms (suppliers, distributors or customers). These factors might also work as barriers to their development or as facilitators on the path to improving their performance and enhancing their competitiveness. The implications derived from the incorporation of such elements to the reform of the business environment concern the need of new methods and methodological approaches, such as, among the most relevant, sectoral and value-chain analysis, in addition of traditional tools such as lobbying efforts and technical assistance in policy design.

On the other hand, this approach also makes way for new demands to reform the business environment that relate to specific sectors and/or regions. White (2004) describes the progress achieved in this field by the strategies of a number of donor agencies. For example, GTZ, ILO, the Agricultural and Rural Development Department of the World Bank and JICA have put in practice regional approaches, while DFID has explored the sectoral dimension14. This paper suggests that the progress achieved in this sphere should extend to the rest of the Committee of Donor Agencies for Small Enterprise Development, by means of initiatives to develop systemic methodologies to deal with the business environment, thus guaranteeing more comprehensive

14 Based upon the suggested approach, these initiatives should also include micro-level elements in their environment-reforming interventions.
interventions. However, these efforts should also consider interventions at the sectoral and/or regional level, making it possible to accumulate the experience of other areas working towards SME development, such as the BDS.

These suggestions, however, evidence the need for greater SME specialization in areas of the business environment or, alternatively, the need for a closer relationship among the different spheres within donor agency structures that might pave the way for systemic approaches. In any case, it should be noted that this proposal seeks to be a complement, not a substitute, of the approaches discussed here.
### Table 1. Approaches for Improving the Business Environment

<table>
<thead>
<tr>
<th>Theoretical Support</th>
<th>Objectives</th>
<th>Tools</th>
<th>Environment Barriers and Spheres</th>
<th>Actions</th>
<th>Modifications intended</th>
<th>Actors</th>
</tr>
</thead>
<tbody>
<tr>
<td>I</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>• The role of the State vs. the market</td>
<td>Raise awareness of the relevance of SMEs and the need for an institutional framework to promote its development</td>
<td>General theoretical reflection on the political, institutional and legal conditions that prevail in the region</td>
<td>The cost of compliance with regulatory frameworks exceeds firm profitability</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>• Macroeconomic stabilization</td>
<td>Develop concrete proposals for solving the issues related to the business environment (domestic level)</td>
<td>International better practices on public policy and promotion programs</td>
<td>Diagnose the barriers in the business environment (methodology)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>• Institutional reform</td>
<td>Classify SME-sector demands</td>
<td>Labor and tax issues</td>
<td>State operation</td>
</tr>
<tr>
<td></td>
<td>Systemic approach (meso level)</td>
<td>• Systemic approach (meso level)</td>
<td>Regional, sectoral and value chain approach (micro level) to solving environment issues</td>
<td>Regional, sectoral and value chain approach (micro level) to solving environment issues</td>
<td>Value-chain analysis</td>
<td>Productive chains</td>
</tr>
<tr>
<td></td>
<td>III</td>
<td></td>
<td>• Systemic approach (micro level)</td>
<td>Productive integration</td>
<td>Local development</td>
<td>Local development</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>o Systemic approach (micro level)</td>
<td>o Productive integration</td>
<td>o Regional, sectoral and value chain approach (micro level) to solving environment issues</td>
<td>o Value-chain analysis</td>
</tr>
<tr>
<td></td>
<td>III</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Notes:**
- The table categorizes approaches into theoretical support, objectives, tools, environment barriers and spheres, actions, modifications intended, and actors involved.
- The approaches are organized into three levels: macroeconomic (I), systemic (meso) (II), and productive integration (III).
- Each level outlines specific strategies for improving the business environment, focusing on both theoretical and practical interventions.
- The table highlights the importance of considering different spheres such as finances, infrastructure, and labor, as well as the need for institutional frameworks.
- Actors are identified across various roles including experts, scholars, policymakers, and decision makers.
References


Bravo, D., et.al (2002) Desarrollo se escribe con PYME. El caso chileno. FUNDES Chile


FUNDES (2004) 20 años Impulsando a las PYME de América Latina, FUNDES Internacional, San José, Costa Rica


Torres González, E., et.al. (coord.) (2002) Retos y Oportunidades del Financiamiento a la Empresa Media, FUNDES México

