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Report IV

Small and medium-sized enterprises and decent and productive employment creation



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Report IV

Small and medium-sized enterprises and decent and productive employment creation

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Executive summary

The purpose of this report is to provide delegates to the 104th Session of the International Labour Conference with up-to-date evidence on the relevance of small and medium-sized enterprises (SMEs) for employment, the key constraints faced by SMEs and their workers, and the effectiveness of measures to support this enterprise segment. The report ultimately attempts to provide answers to crucial questions such as whether SMEs are living up to their promise of being a major contributor to job creation, whether these jobs are of adequate quality, and how effective the various policies for promoting SMEs are.

Are SMEs a major job creation engine?

There is solid empirical evidence confirming that SMEs are a major job creation engine. However, the analysis also clearly shows that the sector is very diverse. This is a serious obstacle to policy formulation for this enterprise size class as a whole. There is a risk that promoting SMEs because of their large contribution to employment, without further differentiating them by sub-segments, may result in a trade-off between the quantity and quality of employment, because SMEs also include a large number of micro-enterprises that create jobs that are neither productive nor decent.

Moreover, the data presented from developed countries show that entrepreneurial activities and the corresponding employment creation are more closely related to the age of the enterprises than to their size per se. It is especially young small enterprises that make disproportionately high contributions to employment.

Even within SMEs in the large informal economy in developing countries, the same heterogeneity, and hence the same need for policy differentiation, can be found. In contrast to the prevailing view that the informal enterprise segment consists only of subsistence entrepreneurs, there is in fact a sizeable higher tier of growth-oriented informal enterprises that can make significant contributions to employment generation. Nevertheless, it is important to note that most SMEs in developing countries are low-productivity informal micro-enterprises that will not grow and create additional jobs.

A key consequence for policy-making is that policies for SMEs need to be based on a better differentiation between the heterogeneous parts of the size group. Specific measures should be considered for young, growing enterprises, alongside evaluations of whether the expected positive quantitative and qualitative effects on employment are achieved. At the same time, support for micro-enterprises should be continued, since they play an important role in providing incomes and livelihoods, especially where there is a lack of sufficient wage employment.

What are key constraints faced by SMEs and their workers?

The constraints to SME growth – as perceived by business owners – is a relatively well-researched area. The three biggest constraints across countries are access to finance, access to electricity and competition from informal enterprises. However, constraints vary according to countries' level of development as well as by region. There is a need to continuously update this information through representative enterprise surveys, as has been done by the ILO and others, in order to maintain and expand the foundation for an evidence-based policy dialogue.

Much less is known about the problems or disadvantages that are faced by workers in SMEs. The only solid data come from the European Union (EU), and they show that SMEs generally score lower than large enterprises in indicators of the quality of employment. No data are available for low- and middle-income countries. This situation has three implications. First, it highlights the need for more data to be collected on the quality of employment in SMEs. Second, the available findings that the quality of employment is lower in SMEs should not lead to an abandonment of SME promotion; their contribution to job creation is too important. Instead, the objective should be to support SMEs in increasing their productivity and improving the quality of jobs. With that in mind, the ILO has made productivity and working conditions in SMEs one of its new areas of critical importance. Third, an important finding from the available data is that the economic sector in which an SME operates has a stronger influence on the quality of employment than the size of the enterprise. It might thus be more effective to focus on specific sectors rather than on enterprise size segments when designing future interventions to improve the quality of employment.

Employers' and workers' organizations can play an important part in helping SMEs and their workers to overcome the constraints that they face. Increasing the representation of SMEs in both types of organization will help to further strengthen their role as advocates for this enterprise segment. Social partners also provide a variety of important services to their members that can be beneficial for SMEs. These services include information, training, guidance on how to access public and private business support services, links to research and consultancy resources, business matchmaking and advice on responsible workplace practices. Employers' organizations should continue to periodically assess the enabling environment through enterprise surveys, business barometers and other tools. Workers' organizations should provide services and advice on workers' rights and obligations, labour legislation and social protection for workers in SMEs.

What SME policies do work?

It is clear that a range of important economic and social policies, such as those centred on macroeconomics, infrastructure or social protection, have a substantial impact on SMEs. However, these policies are not the focus of this report, since they do not specifically target one size class of enterprises to the exclusion of others. The focus of this report is SME policies, defined as any public initiative targeted at promoting existing enterprises below a certain size. The two main economic justifications for SME policies are: (1) to address market failures specific to this size segment; and (2) to promote the special economic contributions of SMEs, especially in terms of employment creation. While there is broad agreement over the existence of market failures, there are conflicting views on the special economic contributions made by SMEs. The best way to

make progress is to undertake more quantitative impact evaluations of SME policies. This will allow policy-makers to track the results, compare the costs with the associated economic and social benefits, and assess the efficacy of SME policies compared to other interventions that do not target enterprises below a certain size. Promoting an evaluation culture is also important, since governments, non-governmental organizations and donors continue to spend considerable budgets on SME policies. Therefore, the report focuses on summarizing the available evidence on the effectiveness of the most important SME policies in terms of demand from ILO member States.

Access to finance and entrepreneurship training can contribute to income generation and the creation of more and better jobs, especially when they are provided as a package. The majority of the interventions assessed so far have been aimed at micro-enterprises or self-employed people at the bottom of the pyramid. These programmes should be maintained, since they make valuable contributions to providing steady income and creating additional employment. Rigorous impact assessments of SME policies beyond micro-enterprises are scarce and more needs to be done to assess the effectiveness of policies targeting this sub-segment. Such assessments should include the group of young and fast-growing SMEs that creates most of the new jobs. Regarding specific target groups in the labour market, the employment effects of interventions directed at young people are greater than those targeted at other age groups. Hence, youth entrepreneurship should continue to feature among the active labour market policies for combating youth unemployment. Interventions targeting women entrepreneurs appear to be less successful in terms of income and employment generation. This finding calls for a revision of current approaches in order to better address the specific constraints faced by women entrepreneurs. The ILO is already a major player in supporting entrepreneurship development and has made considerable efforts and investments to rigorously assess its interventions in this area. Evaluations of the impact of ILO interventions show a strong performance with regard to income generation, but a mixed picture concerning employment creation. However, it is clear that more assessments are needed. These should also go beyond the current focus on income generation and produce additional data on the quality of employment. Future assessments should also include cost–benefit analyses, something which the ILO, and indeed most other agencies, have not undertaken to date.

There is solid evidence that an **enabling environment** supports employment and economic growth, and that the smaller the enterprise, the greater the effects on employment. This confirms the assumption that a favourable environment and a level playing field are important for the development of SMEs. The ILO's own work on an enabling environment for sustainable enterprises (EASE) does not yet have a sufficiently long history to be able to present results on the impacts. There are, however, promising initial results on the intermediate outcomes, such as the adoption of reforms and reductions in bureaucracy. The ILO will need to expand its efforts to monitor and quantify the results of its enabling environment interventions.

Formalization of informal SMEs is highly relevant for the ILO's broader approach to facilitating the transition from the informal to the formal economy. Formalization is seen as a means of breaking the vicious circle of low productivity and precarious working conditions prevailing in the informal economy. Empirical evidence on what works and what does not work to formalize SMEs is still scarce. Overall, the effects of formalization interventions on levels of formality, enterprise performance and employment are modest. The limitation of this finding is that evaluations have mostly focused on business entry reforms. Successful case studies suggest that interventions need to go beyond reducing the cost for enterprises to become formal and also offer a

reduction in the costs and/or an increase in the benefits of being formal. Offering simplified tax schemes or social security provision might increase formalization. Additional research experimenting with different combinations of cost reductions, extended benefits and strengthened law enforcement is needed.

Concerning interventions to **improve working conditions and SME productivity**, the key finding is that a greater integration of initiatives to improve working conditions and to upgrade core management practices is needed. There is considerable evidence that a systemic approach that elevates and integrates working conditions into the core operations of a business can produce better results than stand-alone interventions that seek to improve a single aspect of working conditions. More research is needed to test the effectiveness of integrated packages of connected practices.

Value chain development interventions are becoming increasingly popular because of their strong emphasis on scale and financial sustainability. While there has so far been no rigorous evidence on the effectiveness of these interventions, a recently launched ILO knowledge generation project focuses on measuring the labour market effects of value chain interventions and on testing different results measurement systems. This should help to close the knowledge gap within the next two years.

The report identifies a number of **new trends in SME policies**. (1) Rigorous monitoring and results measurement have become a key trend. Credible measurements of intermediate outcomes and final impacts are crucial to enable agencies such as the ILO to provide evidence-based policy advice on what works and what does not work and for the ILO to remain a partner of choice. (2) Partnerships with businesses are of interest, since they are expected to increase outreach and improve the sustainability of interventions. However, demonstrating the additional value of partnerships with businesses remains a challenge. The ILO has recently started to increase its direct engagement with enterprises. (3) Greening the business operations of SMEs or supporting them in entering new markets for green products or services are areas of rapidly growing importance. In view of the considerable public and private resources being invested, it is important to develop clear theories of change and solid results measurement frameworks to support SMEs effectively. (4) The new trend towards designing programmes to foster high-growth enterprises requires technical expertise on subjects such as mentorship, physical incubation and angel investors, which the ILO does not yet have. The ILO should test this new approach and build up in-house expertise.

Validity of earlier ILO Recommendations, synergies with other ILC discussions, and alignment with new ILO priorities

In 1998, the International Labour Conference (ILC) adopted the ILO's Job Creation in Small and Medium-Sized Enterprises Recommendation, 1998 (No. 189). It is the only ILO Recommendation that deals specifically with SMEs. Its aim is to provide guidance for Members in the design and implementation of policies on job creation in SMEs. The analysis presented in this report shows that the issues and strategies outlined in Recommendation No. 189 are still valid.

With regard to other ongoing or forthcoming ILC discussions, the report identifies synergies with the standard-setting discussion on the transition from the informal to the formal economy and the upcoming 2016 general discussion on decent work in global supply chains. Concerning the transition to the formal economy, this report collects and

analyses the available data on informal enterprises and documents the evidence on the effectiveness of measures to formalize enterprises. It also highlights the need for a policy response that differentiates between the various types of informal enterprises. For example, growth-oriented informal enterprises might benefit more from formalization than subsistence entrepreneurs. Furthermore, start-ups should be targeted, since they are easier to formalize than existing informal enterprises. As to the forthcoming discussion on decent work in supply chains, it might be important for the Office to consider taking into account sectoral differences in the constraints faced by enterprises and workers. It would seem that sectoral considerations are more significant than differences resulting from enterprise size. This finding underlines the importance of a sectoral approach to the improvement of working conditions.

SME policies can help the ILO to achieve its priorities as defined in the new strategic framework for 2016–17.¹ As shown in table 1, SME promotion can make substantial direct contributions to five out of the ten Office-wide outcomes² by creating additional income and new and better jobs.

Table 1. SME promotion and ILO priorities

New ILO priorities	Contributions of pro-SME interventions
More and better jobs for inclusive growth and improved youth employment prospects	Highly relevant because of the impact on job creation, especially youth entrepreneurship development, enabling environment and value chain development.
Promoting sustainable enterprises	SME policies are key offerings of the enterprise development portfolio and account for 70 per cent of the extra-budgetary resources mobilized.
Decent work in the rural economy	Highly relevant because of the impact on income generation and job creation, especially value chain development.
Formalization of the informal economy	Highly relevant because of the large number of informal SMEs in developing countries; formalization of informal SMEs can contribute to the ILO's broader approach to facilitating the transition from the informal to the formal economy.
Creating and extending social protection floors	Provision of social security to owners and workers of SMEs; can also lead to better enterprise performance if working conditions are integrated into the core operations of the enterprises.

¹ In the ILO's new strategic framework for 2016–17, the total number of outcomes has been reduced to ten, reflecting changes in the ILO's priorities for action and support.

² The other strategic outcome areas to which SME promotion will indirectly contribute are: ratification and application of international labour standards, promoting workplace compliance through labour inspection, protecting workers from unacceptable forms of work, promoting fair and effective labour migration policies, and strong and representative employers' and workers' organizations.

Chapter 1

Introduction

1.1. Context

1. Small and medium-sized enterprises make crucial contributions to job creation and income generation; they account for two-thirds of all jobs worldwide. Therefore, the promotion of SMEs has been a key area of intervention for the ILO. Its advisory services on SME policies are in high demand among ILO member countries. This demand has become even stronger in recent years in view of the major employment challenges in many developing and developed countries. Many international agencies are working on SME promotion, and the ILO is perceived as an important partner. It provides added value because of its focus on both the quantitative and qualitative aspects of employment creation and the fact that it serves constituents that provide a large potential outreach.

2. Against this background, the 104th Session (2015) of the International Labour Conference will hold a general discussion on the opportunities and challenges of SME promotion under the title “Small and medium-sized enterprises and decent and productive employment creation”. The purpose of this report is to provide Conference delegates with up-to-date evidence on the relevance of SMEs, key constraints faced by them and their workers, and the effectiveness of SME policies, as a basis for their discussion. The report also attempts to answer the crucial questions of whether SME promotion is warranted on the grounds that SMEs are living up to their promise of being a major contributor to employment creation and whether the quality of these jobs is adequate.

3. The report builds on previous ILO Recommendations, conclusions and discussions on enterprise development and SME promotion. These include the Job Creation in Small and Medium-Sized Enterprises Recommendation, 1998 (No. 189), and the Conclusions concerning the promotion of sustainable enterprises adopted at the 96th Session of the International Labour Conference (2007).

1.2. Structure of the report

4. The report is divided into six chapters. After a brief introduction (Chapter 1), Chapter 2 presents the latest empirical evidence concerning the contribution of SMEs to employment and economic growth. Chapter 3 highlights the constraints faced by SMEs and their workers. Chapter 4 provides a definition of SME policies, explains the rationale behind them and shows linkages to other important policies. Chapter 5 is the core part of the report and discusses the relevance and effectiveness of the most important types of SME policies in supporting ILO priorities. This includes a summary of the available global evidence as well as the results of ILO interventions. The chapter

ends with an overview of the latest trends in SME policies. Lastly, Chapter 6 suggests points for discussion.

1.3. Definitions

5. Definitions of SMEs often vary by country and are usually based on the number of employees, the annual turnover or the value of assets of enterprises. Typically, micro-enterprises are defined as enterprises with up to ten employees, small enterprises as those that have ten to 100 employees, and medium-sized enterprises as those with 100 to 250 employees. Unless otherwise specified, the definition of an SME that is used in this report is any enterprise with fewer than 250 employees. This includes all types of enterprises, irrespective of their legal form (such as family enterprises, sole proprietorships or cooperatives) or whether they are formal or informal enterprises. For the sake of readability, the report uses the term SME throughout, unless a differentiation of sub-segments is needed.

Chapter 2

Contribution of SMEs to employment and economic growth

6. This chapter presents empirical evidence on the contribution that SMEs make to employment, job creation, productivity, income and economic growth. The focus is on formal enterprises, since there is a lack of consistent time series data on informal enterprises across countries.

7. The data available confirm the predominant role that SMEs play, in that they account for the largest share of both employment and job creation. This is true for developing and developed countries alike, although the share of employment varies considerably between countries. In contrast, the productivity of SMEs is on average a third, and wages half, of the level in large enterprises.

2.1. Contribution of SMEs to employment

8. The contribution made by SMEs to employment was analysed in a study by Ayyagari et al.¹ combining different waves of the World Bank Group Enterprise Surveys.² Their data include information for 99 countries covering the period from 2006 to 2010, making this the most comprehensive study to date. However, one limitation of the study is that it only covers the formal non-agricultural private economy and excludes micro-enterprises. Thus, a large number of SMEs are not covered by the analysis presented here.³ In a study by the ILO and the German Agency for International Cooperation (GIZ),⁴ the data from Ayyagari et al. were further analysed to estimate the share of employment of the SME size class in developing countries. The results show that SMEs have a large share of employment in all countries, irrespective of the countries' income level (figure 2.1) or region (figure 2.2), and is especially high in developing countries. The median share of employment of the SME size class is 67 per cent. No disaggregation by main sectors is available.

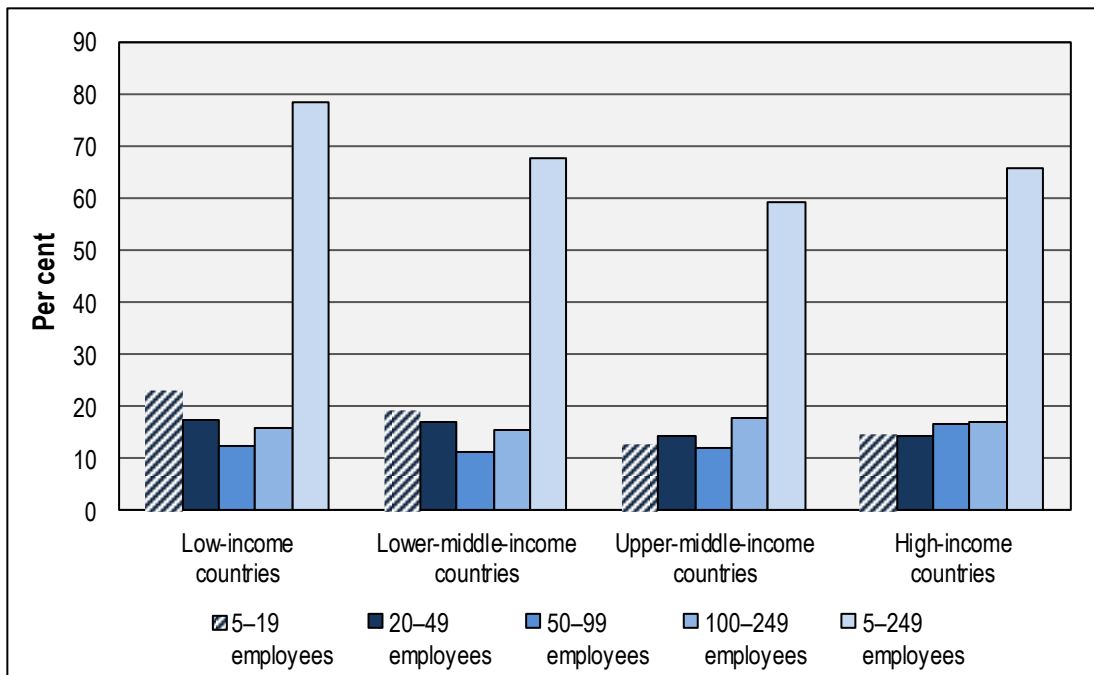
¹ M. Ayyagari, A. Demirgüç-Kunt and V. Maksimovic: *Small vs. young firms across the world: Contribution to employment, job creation, and growth*, World Bank Policy Research Working Paper No. 5631, 2011.

² The World Bank Group Enterprise Surveys provide the world's most comprehensive company-level data in emerging markets and developing economies. Business data collected from face-to-face interviews with managers and business owners are available for 130,000 enterprises in 135 countries.

³ See also the estimates on informal SMEs presented in this chapter.

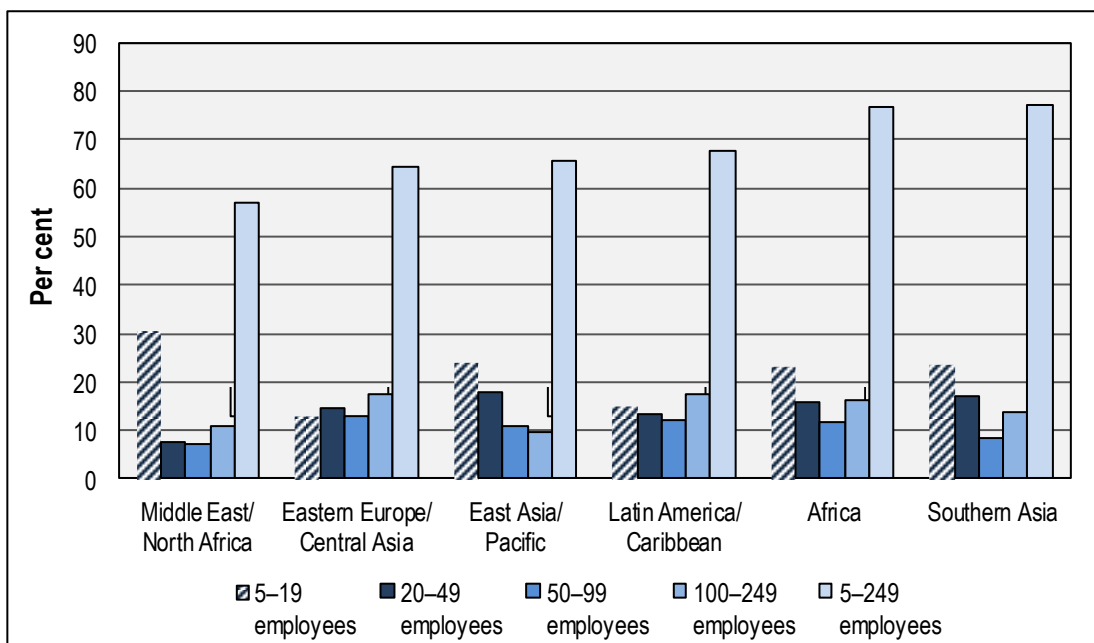
⁴ J. De Kok, C. Deijl and C. Veldhuis-Van Essen: *Is small still beautiful? Literature review of recent empirical evidence on the contribution of SMEs to employment creation* (Eschborn and Geneva, GIZ and ILO, 2013).

Figure 2.1. Median share of employment according to enterprise size class by country income group (per cent)



Source: De Kok et al. (2013), based on Ayyagari et al. (2011), table 2.

Figure 2.2. Median share of employment according to enterprise size class by region (per cent)



Source: De Kok et al. (2013), based on Ayyagari et al. (2011), table 2.

9. The evidence also confirms that SMEs have a majority share in employment in member countries of the Organisation for Economic Co-operation and Development (OECD).⁵ A sample of 18 OECD countries shows that SMEs, including micro-enterprises, account for 63 per cent of total employment, with large enterprises accounting for the remaining 37 per cent.

2.2. Number of SMEs in the total enterprise population, in the informal economy, and those owned by women

10. SMEs account for over 95 per cent of all enterprises in OECD countries.⁶ It is estimated that there are 420 to 510 million SMEs worldwide, of which 9 per cent are formal SMEs (excluding micro-enterprises) and 80–95 per cent are in low- and middle-income countries (see figure 2.3 and table 2 below). According to ILO statistics based on data from 40 countries and limited to non-agricultural employment, there are approximately 375 million people in informal employment (29 per cent of whom are women and 71 per cent men). Of these, 156 million are self-employed in the informal economy and form part of informal enterprises (34 per cent women and 66 per cent men).⁷ Despite a lack of detailed data on informal enterprises⁸ and variations in the definitions of informality, it is clear that the number of informal enterprises is high and that they account for a large share of all SMEs. In some developing countries, informal SMEs far outnumber formal enterprises of the same size. India, one of the few countries with reliable data on informal enterprises, reported 17 unregistered SMEs for every registered SME in 2007.⁹

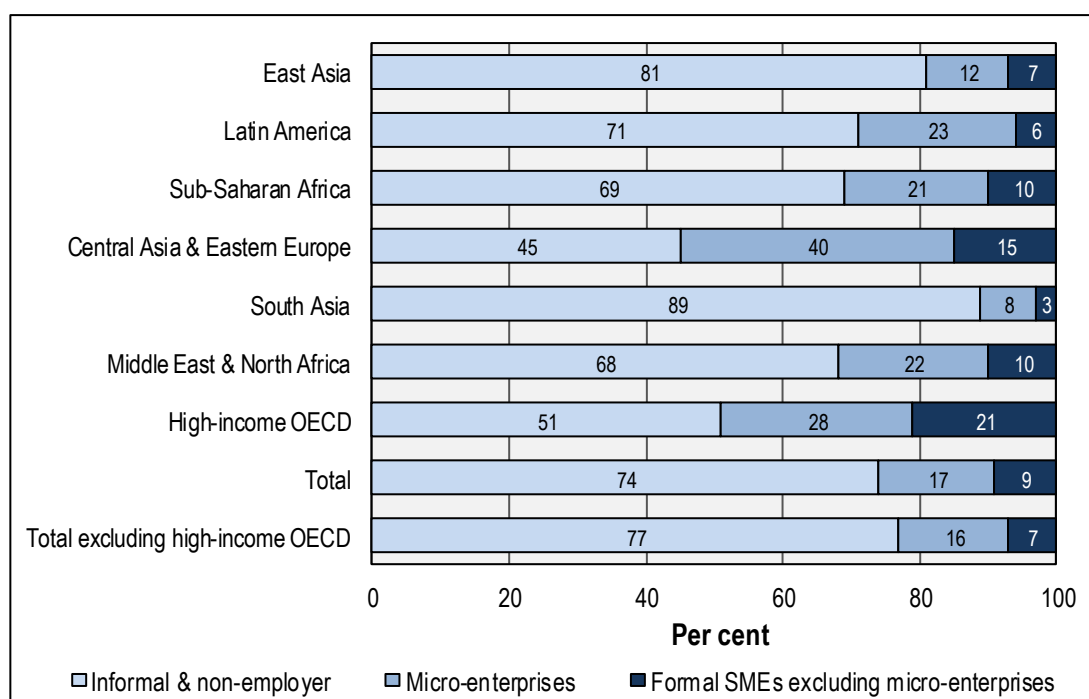
⁵ C. Criscuolo, P.N. Gal and C. Menon: *The dynamics of employment growth: New evidence from 18 countries*, OECD Science, Technology and Industry Policy Papers, No. 14 (2014).

⁶ OECD: *Small and medium-sized enterprises: Local strength, global reach*, OECD Policy Brief (Paris, 2000). The share of SMEs in the total enterprise population is even higher for developing countries.

⁷ Sources: ILO Department of Statistics; country responses to ILO data request, special tabulations of labour force survey data, and extracts from survey reports. For Latin American countries, ILO/SIALC household survey micro-database.

⁸ Note that the category of informal SMEs in figure 2.3 includes not only informal SMEs defined as non-registered enterprises but also registered and non-registered non-employer enterprises (one-person enterprises), which might overstate informality to some extent.

⁹ K. Kushnir, M.L. Mirmulstein and R. Ramalho: *Micro, small, and medium enterprises around the world: How many are there, and what affects the count?* World Bank/IFC MSME Country Indicators (Washington, DC, 2010).

Figure 2.3. Estimated share of SMEs worldwide by region

Source: IFC: *Scaling-up SME access to financial services in the developing world* (Washington, DC, 2010).

Table 2. Estimated number of SMEs worldwide by region

Region	No. of SMEs in region (million)	Percentage of total SMEs worldwide	Total formal SMEs (million)
East Asia	170–205	44–46	11–14
Latin America	47–57	10–12	3–4
Sub-Saharan Africa	36–44	8–10	3–5
Central Asia and Eastern Europe	18–22	3–5	2–4
South Asia	75–90	16–20	2–3
Middle East and North Africa	19–23	4–6	1–3
High-income OECD countries	56–67	12–14	11–14
Total	420–510	100	36–44
Total excluding high-income OECD countries	365–445	80–95	25–30

Source: IFC: *Scaling-up SME access to financial services in the developing world* (Washington, DC, 2010).

11. Reliable and up-to-date information on the number of SMEs owned by women is scarce. Data are available for only a few, mostly OECD, countries. Furthermore, these data are not directly comparable with those from the other sources used in this chapter. In the EU, 25 per cent of all workers in the category of “self-employed with employees” are women.¹⁰ The proportions are similar in Brazil, Canada, Chile, Japan, Republic of Korea, Mexico and United States. Moreover, this relatively low share of women

¹⁰ All data in this and the following paragraph are taken from OECD: *Closing the gender gap: Act now* (Paris, 2012).

entrepreneurs has grown only marginally over the last decade, with the exception of Chile, Republic of Korea and Mexico, which have seen marked increases in the share of female entrepreneurs from a relatively low level (less than 20 per cent) in 2000.

12. The OECD–Eurostat Entrepreneurship Indicators Programme shows a similar picture. This programme has started to collect internationally comparable data on female entrepreneurship based on sole-proprietor enterprises owned by women. The proportion of individually owned enterprises with a female owner varies between 20 and 40 per cent and is on average 25 per cent. However, the number of enterprises owned by women is growing faster than those owned by men. In terms of enterprise performance, there is no gender gap with regard to enterprise survival or employment creation. Men- and women-owned sole-proprietor enterprises have similar survival rates and make similar contributions to job creation in the first three years after start-up. However, there is a large difference in the size of the operations as measured by sales or value added. The average turnover of enterprises owned by women is only a fraction of those owned by men: for example, it is 38 per cent in Mexico, 26 per cent in Italy and 18 per cent in the Netherlands. It is not entirely clear whether this is due to women’s preferences for certain sectors and occupations or to gender-specific constraints faced by women when starting and growing an enterprise.

13. For developing countries, the International Finance Corporation (IFC) estimates that there are 8–10 million formal SMEs owned by women, which represents roughly a third of all formal SMEs.¹¹ Female entrepreneurship is skewed towards smaller enterprises. A third of very small enterprises are owned by women and only 20 per cent of medium-sized enterprises. It is generally assumed that female entrepreneurs are more likely to operate in the informal economy, as it is often the only source of employment for low-skilled and poor women who have to work from home in order to balance business and family commitments. However, no solid global data are available. The World Bank estimates that globally more than 30 per cent of women in the non-agricultural workforce are engaged in self-employment in the informal economy. This figure is as high as 63 per cent in Africa.¹²

14. Based on the above, it is clear that more data is needed to monitor and interpret trends in women-owned SMEs. However, it is safe to assume that these enterprises represent a significant share of the total SME population and make important contributions to employment and income generation.

2.3. Enterprise size and job creation

15. Beyond their predominance in the share of employment and number of enterprises, SMEs also play a critical role in the job creation process. The direct net job creation of SMEs can be analysed at the level of enterprise size classes.¹³ Net job creation is generally understood to be the difference between the jobs created by new or existing enterprises and the jobs destroyed either through contraction of existing enterprises or through business closures. Thus, the figures cover entries and exits of enterprises, unless specified otherwise.

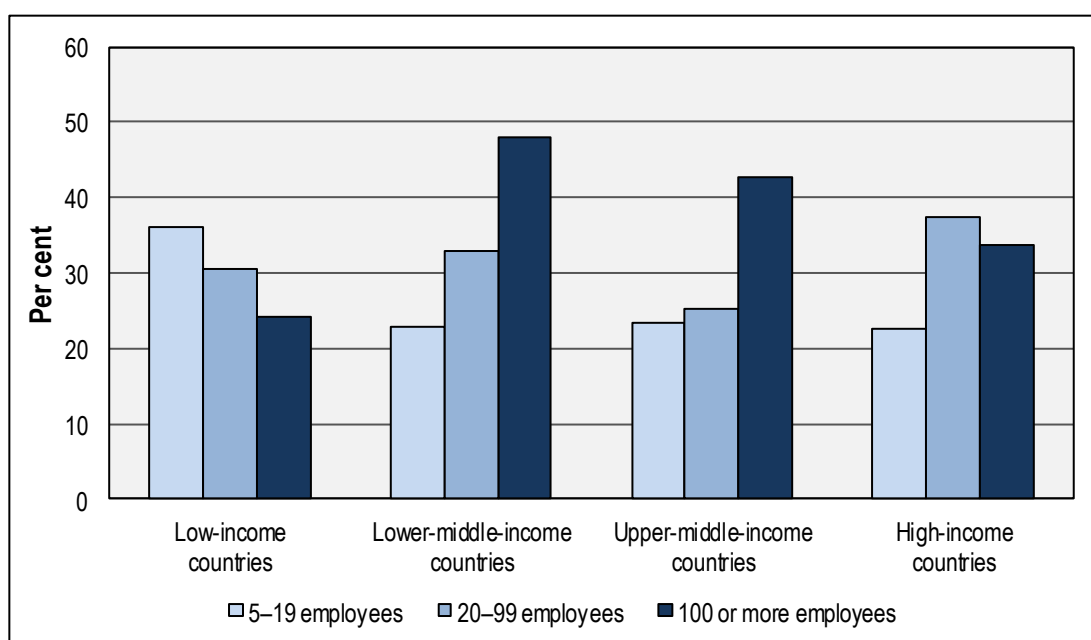
¹¹ IFC, G20 Global Partnership for Financial Inclusion: *Strengthening access to finance for women-owned small and medium-sized enterprises (SMEs) in developing countries* (Washington, DC, 2011).

¹² World Bank: *Female entrepreneurship resource point – introduction and module 1: Why gender matters*, 2013.

¹³ This does not include an analysis of indirect job creation (jobs created by enterprises’ distributors and suppliers within the value chain or through increased innovation and competition) or induced job creation (jobs generated by the consumer spending of new directly employed people) by size class.

16. For the majority of countries, more than 50 per cent of total net employment creation can be attributed ¹⁴ to the smallest size classes of enterprises of between five and 99 employees. ¹⁵ This finding holds for each country income group (figure 2.4); however, no disaggregation by sector is available. As for enterprises with up to 250 employees, there is no unbiased global data. Nevertheless, it can be assumed that the net employment creation of the entire SME segment is significantly higher than the above figure. Data from the EU show that 85 per cent of net employment creation is attributable to SMEs with between one and 250 employees, including enterprise entries and exits. ¹⁶ During times of economic downturn, the picture changes. Employment in SMEs seems to be less resilient to economic crises. Figures from the EU show that during the Great Recession of 2007–09, the number of jobs in SMEs fell by an average of 2.4 per cent annually, as opposed to 1 per cent in large enterprises. ¹⁷

Figure 2.4. Share of total net job creation by enterprise size class and country income group



Source: De Kok et al. (2013), based on Ayyagari et al. (2013), appendix.

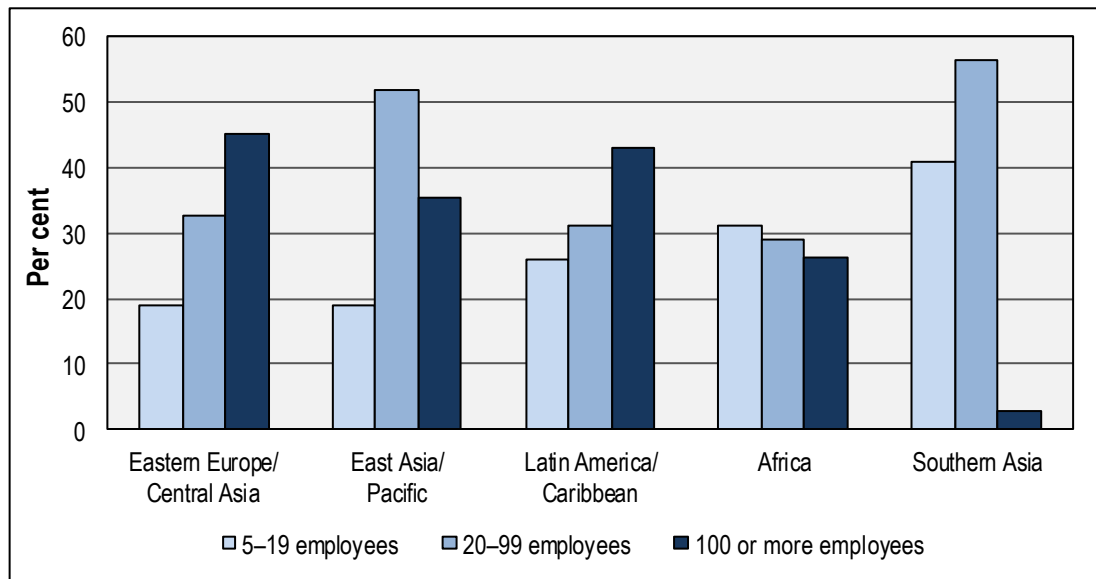
¹⁴ Any method that determines the contribution of different size classes to net employment creation has to account for the fact that enterprises may move from one size class to another. This section only presents statistics based on methods that are not biased towards a specific size class. A more elaborate discussion of this topic can be found in De Kok et al. (2013), op. cit.

¹⁵ M. Ayyagari, A. Demirgüç-Kunt and V. Maskimovic: “Who creates jobs in developing countries?” in *Small Business Economics* (2014, Vol. 43). The limitation of these data from 104 countries is that they cover net job creation over a period of two years (rather than one) and do not cover entry and exit of new enterprises.

¹⁶ J. de Kok et al.: *Do SMEs create more and better jobs?* (Brussels, 2011).

¹⁷ *ibid.*

Figure 2.5. Share of total net job creation by enterprise size class and region



Note: Middle East/North Africa not included due to lack of data.

Source: De Kok et al. (2013), based on Ayyagari et al. (2013).

17. While the employment share of SMEs, as well as their share in net job creation, differs only moderately between low- and high-income countries, there is a strong variation in entry density.¹⁸ This ranges from 0.4 in low-income countries to 6.4 in high-income countries. Entry density may well be a better reflection of the level of entrepreneurship and dynamism in an economy than data on the share of employment or job creation attributable to SMEs, and shows a greater covariation with income level.

18. As figure 2.5 above shows, there are important differences in job growth across regions. In South Asia, there is a low share of job creation by larger enterprises. In Africa, the majority of job creation is by the smallest enterprises (less than 19 employees), whereas in Eastern Europe/Central Asia and Latin America, more than 40 per cent of job creation comes from enterprises with more than 100 employees. In East Asia and the Pacific, job growth is concentrated mainly in enterprises with 20–99 employees.

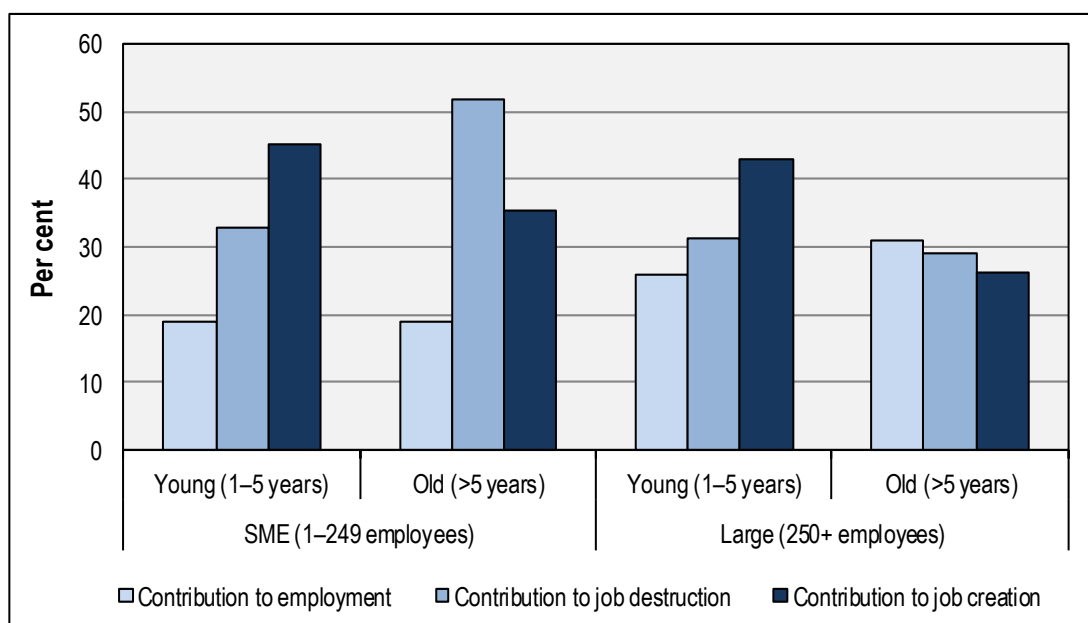
2.4. Relative contribution of young enterprises, start-ups and gazelles

19. It is of particular interest to analyse which subgroups of SMEs have the highest employment growth rates. For their sample of 99 countries, Ayyagari et al. found that small enterprises with fewer than 100 employees and young enterprises (established less than two years ago) have the highest job creation rates. A recent OECD study comes to similar conclusions, showing that young small enterprises create a disproportionately high number of jobs (figure 2.6), with a higher net job creation in the service sector than in manufacturing. Although young enterprises respond more strongly to economic upturns or downturns than old enterprises, they remained net job creators during the

¹⁸ Measured as the number of newly registered limited liability companies per 1,000 people of working age; see Ayyagari et al. (2011), op. cit.

Great Recession of 2007–09. Most of the job losses were caused by contractions of mature businesses.¹⁹

Figure 2.6. Employment, job creation and destruction by enterprise age and size – OECD sample (2001–11)



Source: Criscuolo et al., op. cit. The graph shows the contribution to total employment, gross job creation and job destruction by enterprises in the reported age-size class on average across available years and countries. Sectors covered: manufacturing, construction and non-financial services.

20. The OECD study provides further important insights concerning micro-enterprises. This subsector is of particular importance, as it is the seed-bed of start-ups. Enterprises mostly start as micro or small enterprises, but might grow to become large enterprises. Few start-ups (2–9 per cent) grow above ten employees, but they make a substantial contribution to job creation, ranging from 19 to 54 per cent. **It is ultimately only a few enterprises that grow to become larger enterprises and generate most of the new jobs.** These high-growth enterprises are often referred to as transformational entrepreneurs, graduate enterprises or gazelles, and they create vibrant businesses with jobs and income for others, beyond the scope of an individual’s subsistence needs. In contrast, subsistence entrepreneurs usually do not grow, but provide income and employment for the owner of the micro-enterprise and his or her family.²⁰

¹⁹ Criscuolo et al., op. cit.

²⁰ On transformational and subsistence entrepreneurs, see A. Schoar: “The Divide between Subsistence and Transformational Entrepreneurship”, in *Innovation Policy and the Economy* (2010, Vol. 10), National Bureau of Economic Research. On the history of the gazelles discussion, see T.D. Boston and L.R. Boston: “Secrets of gazelles: The differences between high-growth and low-growth business owned by African American entrepreneurs”, in *The Annals of the American Academy of Political and Social Science* (2007, Vol. 613). On graduate enterprises, see: C. Liedholm and D. Mead: *Small enterprises and economic development: The dynamics of micro and small enterprises* (London, New York, 1999).

21. In the case of the United States, a 2014 study²¹ came to similar conclusions. The analysis of enterprise data of the United States Census Bureau from 1976 to 2011 showed that a small fraction of young small enterprises makes a disproportionately high contribution to job creation. US start-ups (90 per cent of which have fewer than 20 employees) account for less than 10 per cent of enterprises, but 20 per cent of gross job creation. High-growth enterprises – defined as establishments that expand their employment by more than 25 per cent per year, many of which are young enterprises – represent 15 per cent of all enterprises and account for 50 per cent of gross job creation. For a sample of 50,000 SMEs from six developing countries, a 1999 study showed similar trends. Only 1 per cent of all micro-enterprises ever leaves the size class and grows to employ more than ten workers. Yet these high-growth enterprises create a quarter of all new jobs in the SME size class.²²

22. There is little data available on the number of growth-oriented enterprises in the informal economy in developing countries. The prevailing view has been that the informal economy largely consists of subsistence entrepreneurs. Recent research shows that both types of micro-enterprises are present in the informal economy: dynamic enterprises with the ability and potential to grow and necessity-driven enterprises whose owners would probably prefer to be waged and salaried workers. A representative survey of the informal economy in seven urban centres in West Africa shows that 10 per cent of informal enterprises are growth-oriented (top performers) based on enterprise size and productivity criteria. Another third of all informal enterprises are potentially successful enterprises with characteristics similar to those of top performers (business skills, entrepreneurial behaviour and high marginal returns to capital). However, these so-called “constrained gazelles” do not grow, because of a lack of access to finance or other barriers in the enabling environment.²³

23. A recent study analysing whether self-employed people in developing countries are successful entrepreneurs comes to similar conclusions.²⁴ Based on labour-force and household surveys from 74 low- and middle-income countries, the study shows that 10 per cent of self-employed people are successful entrepreneurs, with the measure of success being whether a self-employed worker is an employer, as opposed to an own-account worker. A third of unsuccessful self-employed people share similar characteristics with their successful counterparts, suggesting that they have the potential to become employers but face external constraints on growth. The main conclusion is that there is a sizeable upper tier of growth-oriented micro-enterprises in the informal economy in developing countries that could make significant contributions to employment generation.

24. Based on the above findings, it is clear that monitoring of new enterprise formation is an important topic. This is especially true in situations where there is a decline in entrepreneurship, reflected in a lower rate of creation of new enterprises and an increasing dominance of older enterprises in total employment. One study on the United

²¹ R. Decker et al.: “The role of entrepreneurship in US job creation and economic dynamism”, in *Journal of Economic Perspectives* (2014, Vol. 28-3).

²² Liedholm and Mead, summarized in E. Berner, G. Gomez and P. Knorringa: “‘Helping a large number of people become a little less poor’: The logic of survival entrepreneurs”, in *European Journal of Development Research* (2012, Vol. 24.3).

²³ M. Grimm, P. Knorringa and J. Lay: “Constrained gazelles: High potentials in West Africa’s informal economy”, in *World Development* (2012, Vol. 40, No. 7).

²⁴ T.H. Gindling and D. Newhouse: “Self-employment in the developing world”, in *World Development* (2014, Vol. 56).

States found that private sector employment in enterprises aged 16 years or more increased from 60 per cent in 1992 to 72 per cent in 2011.²⁵ This trend is documented for a broad range of industrial sectors and regions throughout the United States. A similar trend of declining business dynamism can be observed for other OECD countries.²⁶ At present, there are no data from developing countries. This rising share of mature enterprises and declining number of young enterprises is a cause for concern, since young businesses are more innovative, have higher productivity growth rates and tend to create more new jobs. However, neither the causes nor the consequences of this trend are yet fully understood. Explanations include increasingly burdensome regulations and a higher rate of business consolidation, whereby new technologies have come to favour large mature enterprises and large chains with many establishments. The reasons behind this decline in business dynamism remain an empirical puzzle and researchers do not yet have evidence-based explanations.²⁷

2.5. Productivity and wage income

25. Data from World Bank Group Enterprise Surveys confirm that, on average, larger enterprises are more productive (figure 2.7). They benefit from economies of scale and invest more in machinery and skilled workers. They are also more likely to develop new products and make use of outsourcing, which tends to increase productivity. After controlling for age, education and other characteristics of workers, the data also show that large enterprises tend to pay higher wages. In developing countries, the dispersion of productivity across enterprises is further widened by the presence of a large segment of informal enterprises. The World Bank's surveys of informal enterprises show that in Africa the productivity of small formal enterprises is 120 per cent higher than that of informal enterprises, while wages are 130 per cent higher.²⁸ The productivity report of the Inter-American Development Bank points in the same direction, finding that the least productive enterprises tend to be the smallest.²⁹

²⁵ I. Hathaway and R. Litan: *The other aging of America: The increasing dominance of older firms* (Brooking Institution, July 2014).

²⁶ Criscuolo et al., op. cit.

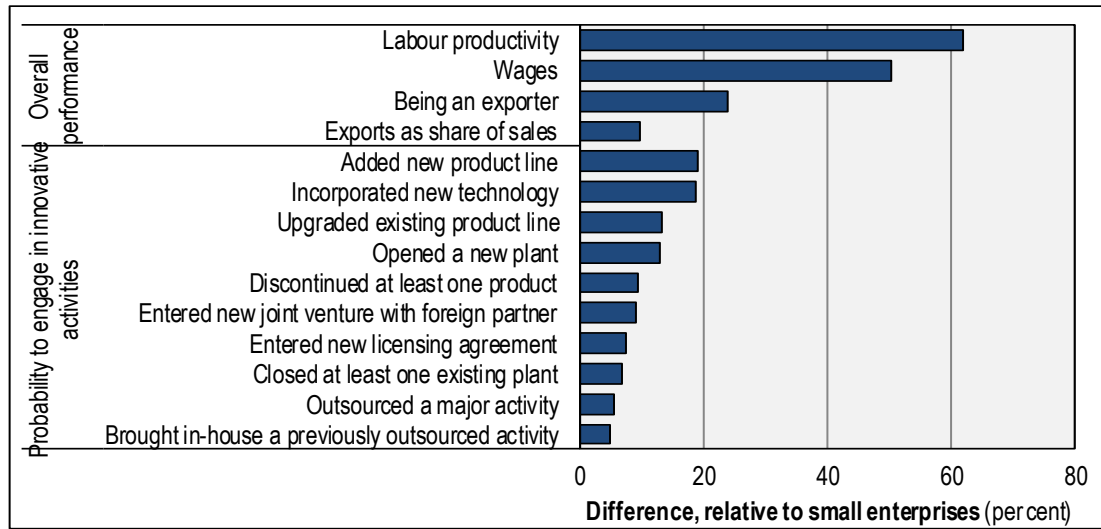
²⁷ Decker et al., op. cit.

²⁸ R. La Porta and A. Shleifer: *The unofficial economy in Africa*, National Bureau of Economic Research Working Paper Series, No. 16821 (Cambridge, Massachusetts, 2011).

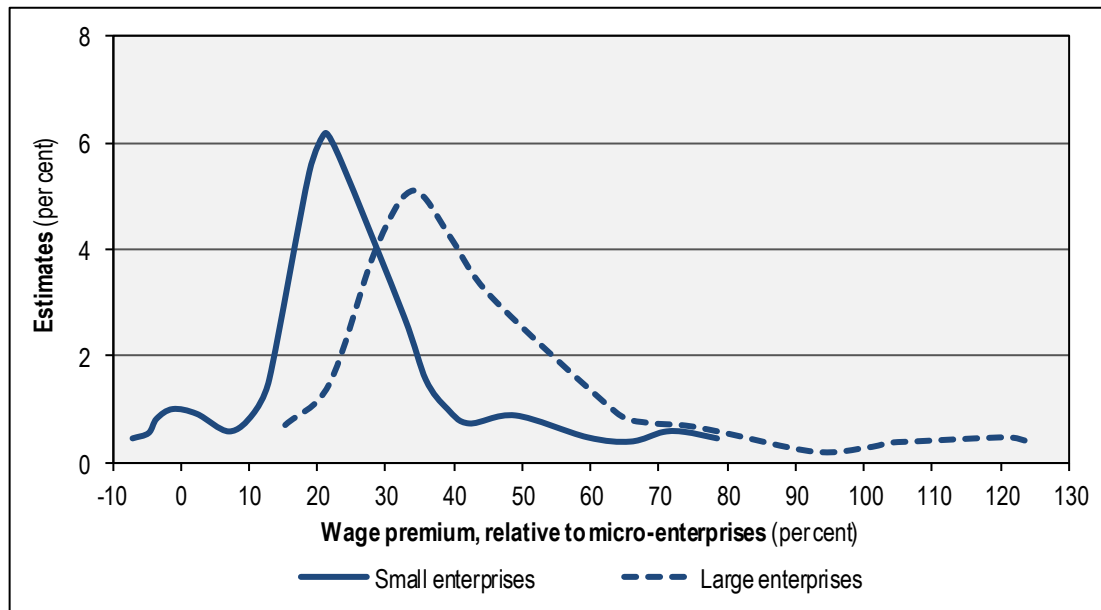
²⁹ C. Pagés (ed.): *The age of productivity: Transforming economies from the bottom up* (Washington, DC, Inter-American Development Bank, 2010).

Figure 2.7. Differences in productivity and wage earnings between small and large enterprises

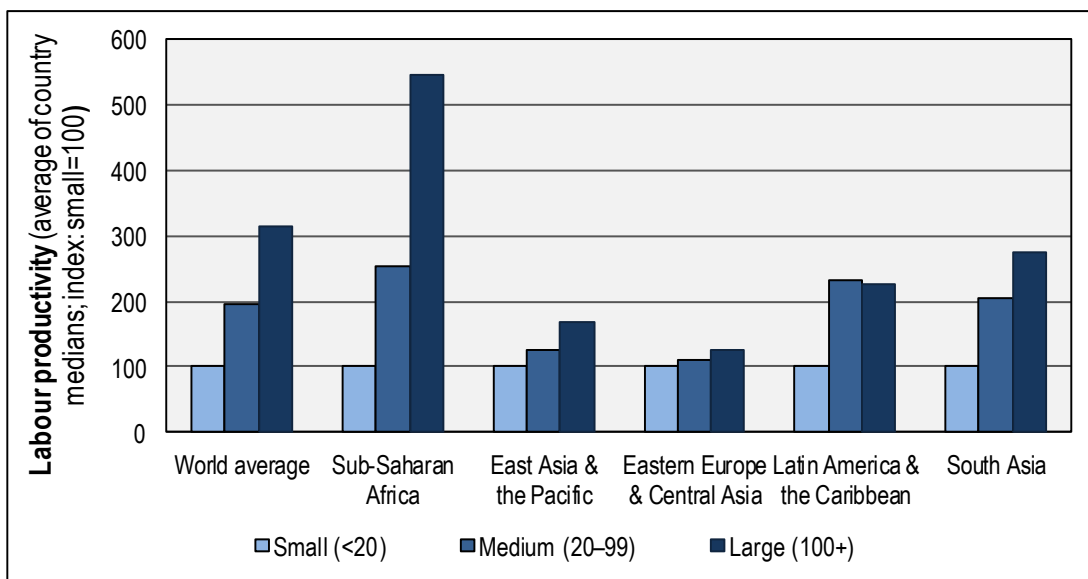
(a) Large enterprises are more productive and innovative



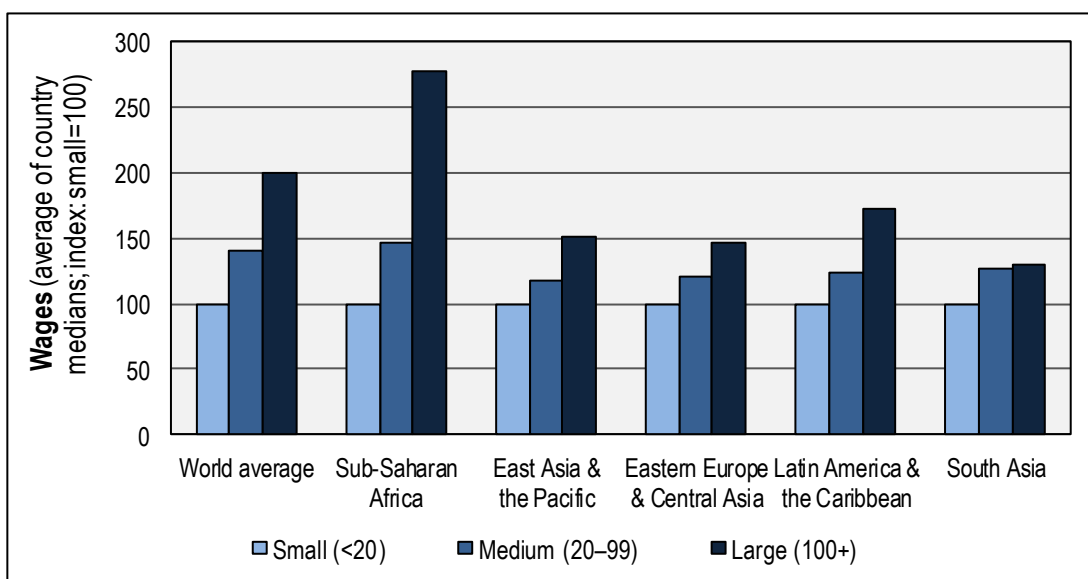
(b) Larger enterprises pay higher wages



(c) **Labour productivity**



(d) **Wages**



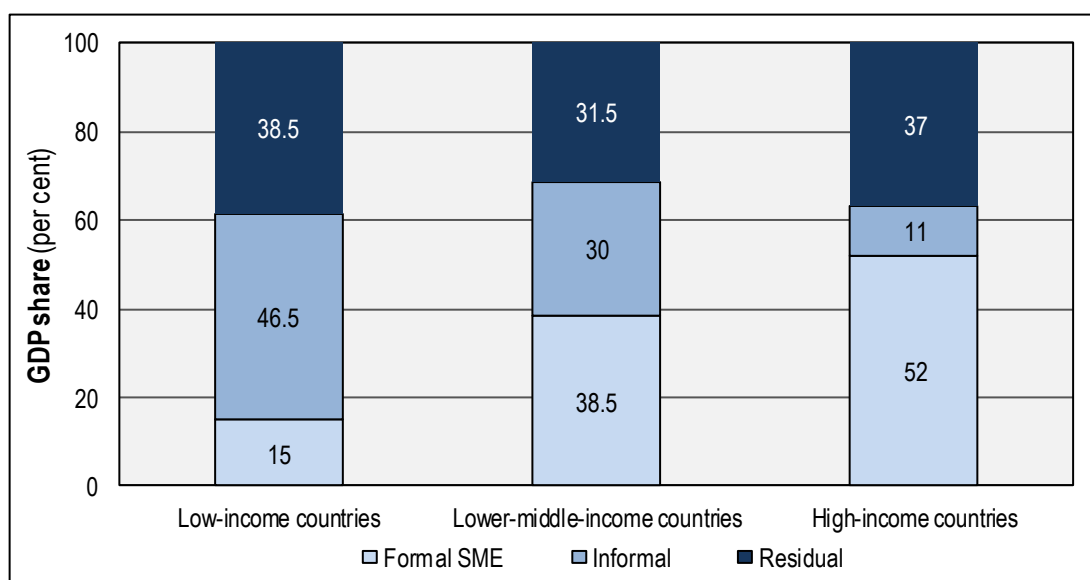
Note: Labour productivity is calculated as total annual sales per full-time permanent employee. Wages are calculated as total annual labour costs divided by the number of full-time permanent employees.

Sources: *World Development Report 2013*; IFC: *Assessing private sector contributions to job creation: IFC open source study (2013)*; World Bank Group Enterprise Surveys.

2.6. Contribution to national income and economic growth

26. Global estimates of the contribution made by SMEs to gross domestic product (GDP) show that this sector, including both formal and informal enterprises, accounts for 60–70 per cent of GDP.³⁰ As can be seen from figure 2.8, the contribution of the informal enterprise segment (mostly micro-enterprises) decreases significantly at higher income levels and there is a marked shift to a larger number of formal SMEs that make a crucial contribution to national income. The phenomenon that developing countries have a large number of micro-enterprises and some large enterprises, but far fewer formal SMEs, is often referred to as the “missing middle”.³¹ This missing middle is seen as the root problem of sluggish productivity increases and low growth rates in developing countries.³²

Figure 2.8. SMEs' share of GDP by country income level



Source: Ayyagari et al., 2003.

27. While there is consistent evidence that a large share of SMEs spurs economic growth at the industry or subnational level,³³ the picture is less clear at the country level. The first cross-country study analysing whether a large share of SMEs has an effect on national economic growth covered 45 developing and developed countries. It found a strong correlation between the size of the SME sector and economic growth, but was unable to establish causality.³⁴ A key limitation of this study is that it only covers the manufacturing sector, where small enterprises are naturally disadvantaged because of

³⁰ M. Ayyagari, T. Beck and A. Demirgüç-Kunt: *Small & medium enterprises across the globe: A new database*, World Bank Policy Research Working Paper 3127 (Washington, DC, 2003).

³¹ See, for example, Harvard Kennedy School, Entrepreneurial Finance Lab Research Initiative: *The missing middle*, 2014.

³² See Pagés (2010), op. cit.

³³ See the literature summarized in D.R. Silivestru: *European SMEs and economic growth: A firm size class analysis*, Annals of the Alexandru Ioan Cuza University – Economics (Vol. 59-2, Cluj, 2013).

³⁴ See T. Beck, A. Demirgüç-Kunt and R. Levine: “SMEs, growth, and poverty: Cross-country evidence”, in *Journal of Economic Growth* (2005, Vol. 10).

economies of scale. Furthermore, the analysis does not deal with productivity or competitiveness. It considers a larger, not a more vibrant, SME sector.³⁵ A recent econometric study covering the then 27 countries of the EU finds a positive, causal relationship between the prevalence of SMEs and economic growth, indicating that on average countries with a larger SME population experience higher growth rates.³⁶ A further study covering 41 upper-middle- and high-income countries suggests that it is large businesses, and not SMEs, that exert the more robust effects on growth. The same study also indicates that excessive reliance on large enterprises has negative effects on growth because of the increasing market dominance of these enterprises.³⁷

28. The SME sector is probably too heterogeneous for one single clear trend to be pinpointed on its contribution to growth. However, differentiating SMEs by enterprise age provides a clearer picture. It is the relatively small subgroup of young dynamic enterprises that makes a key contribution to economic growth. Empirical studies have found a significant relationship between the entry of new enterprises and economic growth.³⁸ Furthermore, entry density in high-income countries is a multiple of the rate in low-income countries (6.4 against 0.4).

2.7. Summing up

29. To summarize this chapter, the empirical evidence available confirms that SMEs are a major job creation engine. However, their productivity and wages are lower than in large enterprises. There is a risk that promoting SMEs because of their substantial contribution to employment, without further differentiating by sub-segments, may result in a trade-off between the quantity and quality of employment, especially in developing countries with a high share of informal micro-enterprises.

30. The analysis shows that SMEs are highly heterogeneous, with opposing trends in the various sub-segments. The prevailing view that SMEs are synonymous with entrepreneurs and job creation and that they therefore merit support seems to be too simplistic. Looking only at enterprise size does not give the full picture of who creates jobs, and might therefore lead to incorrect policy conclusions. The figures presented from advanced countries suggest that entrepreneurial activity and the related job creation are more closely related to the age, rather than the size, of enterprises. Young small enterprises have the highest employment growth rates and make disproportionately high contributions to employment. Therefore, policy-makers should consider offering specific measures targeting these young growing enterprises, and evaluating whether the expected quantitative and qualitative effects on employment are achieved.

31. With regard to developing countries, the SME segment is very often characterized by the presence of a large number of informal micro-enterprises that do not grow, and very few small and medium-sized enterprises (the missing middle). Support for micro-enterprises should not be abandoned, as they often help to provide incomes in situations where wage employment is not available. But, even within the informal enterprise

³⁵ P. Vandenberg: *The relevance of firm size when reforming the business environment*, paper for the Business Environment Working Group, Committee of Donor Agencies for Small Enterprise Development, unpublished, 2005.

³⁶ See Silivestru (2013), op. cit.

³⁷ K. Lee et al.: "Big businesses and economic growth: Identifying a binding constraint for growth with country panel analysis", in *Journal of Comparative Economics* (2013, Vol. 41-2).

³⁸ For a good overview of these studies, see L. Klapper, I. Love and D. Randall: *New firm registration and the business cycle*, World Bank Policy Research Working Paper 6775, 2014.

segment, there is a sizeable upper tier of growth-oriented micro-enterprises that could make significant contributions to employment generation.

32. Ultimately, what is needed is a better segmentation of the heterogeneous SMEs. Each segment serves different purposes, ranging from income stabilization to employment creation and productivity increases, and requires specific interventions.

33. Nor should large enterprises be neglected, since they represent a considerable share of employment and are a major driver of productivity growth. It is also important to note that SMEs and large enterprises do not exist in isolation, but form part of an interacting system, where large enterprises provide SMEs with markets. Furthermore, successful SMEs often begin as spin-offs emerging from large companies or universities.³⁹

³⁹ See P. Nightingale and A. Coad: “Muppets and gazelles: Political and methodological biases in entrepreneurship research”, in *Industrial and Corporate Change* (2014, Vol. 23(1)).

Chapter 3

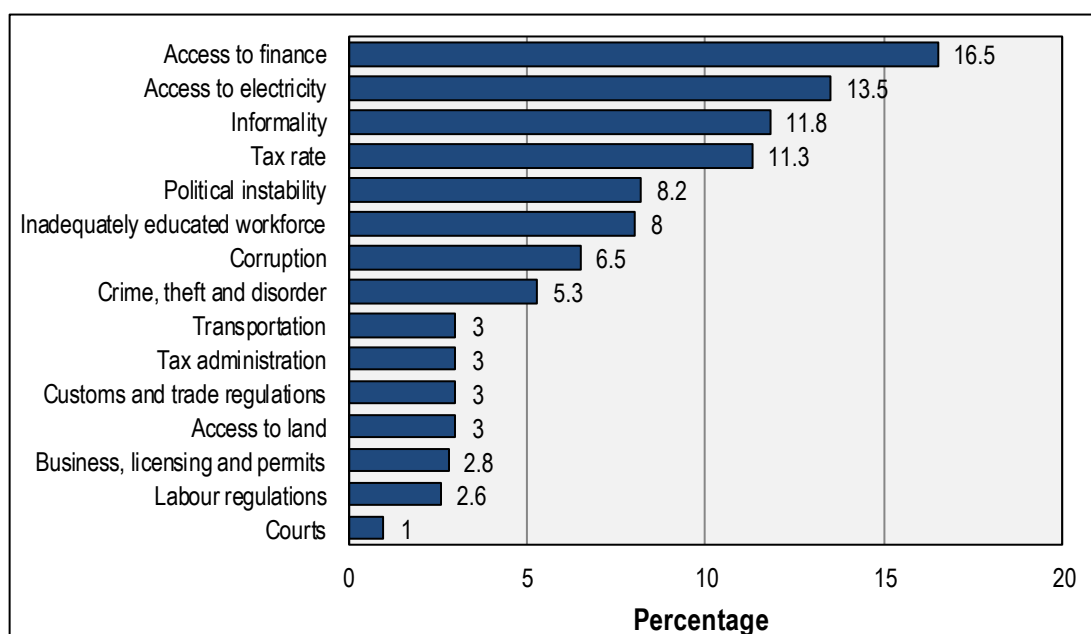
Constraints faced by SMEs and their workers

34. Having identified the contributions made by SMEs to employment, we now turn in this chapter to examine the constraints faced by SMEs and their workers. It is important first to understand what the key constraints are in order to analyse whether and how SME policies can contribute to eliminating them.

3.1. Constraints faced by enterprises

35. The constraints preventing enterprises of all size classes from growing and generating more jobs are relatively well researched. According to data from the World Bank Group Enterprise Surveys,¹ access to finance tops the list of constraints faced by SMEs, with 16 per cent expressing it as their biggest obstacle across countries (figure 3.1).

Figure 3.1. Major constraints faced by SMEs across countries
(percentage of enterprises identifying each of the following factors as being their greatest obstacle)



Source: IFC: Assessing private sector contributions to job creation and poverty reduction, IFC Jobs Study (2013).

¹ The surveys ask owners or managers of enterprises about their perceptions of key constraints. For more information about these surveys see Chapter 2, footnote 2.

36. Access to electricity ranks second, with 14 per cent of SMEs expressing it as their biggest obstacle; competition from the informal economy ranks third, at 12 per cent. Some 42 per cent of all SMEs consider these three obstacles to be the most significant ones. Other important constraints of SMEs are tax rates, political instability, an inadequately educated workforce, corruption and disorder.

37. Large enterprises encounter slightly different constraints across countries, with access to electricity topping their list (15 per cent), followed by a lack of skills of the labour force (12 per cent) and access to finance (11 per cent).

38. There are also differences according to the level of economic development. Access to electricity is the top constraint for enterprises of all size classes in low-income countries (26 per cent), followed by access to finance (21 per cent). Among enterprises in high-income countries, the greatest constraint is inadequate skills of the labour force (18 per cent), followed by tax rates (14 per cent).

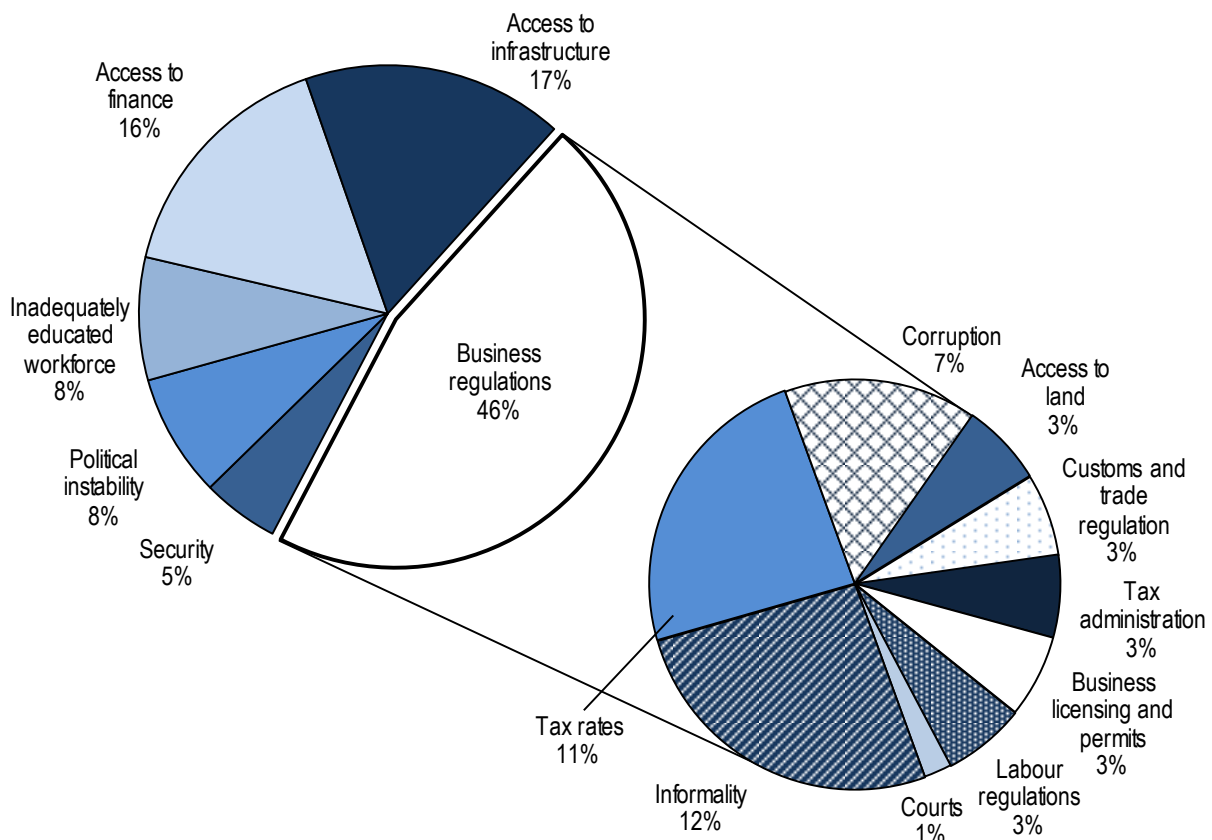
39. The most significant constraints also differ by region. In sub-Saharan Africa, 22 per cent of enterprises of all size classes stated that access to electricity was their biggest obstacle. In East Asia and the Pacific, 17 per cent of enterprises ranked access to finance as their top constraint. In Europe and Central Asia, tax rates were the primary concern (17 per cent). In Latin America and the Caribbean, informality was the principal obstacle (16 per cent); and in South Asia, political instability was the biggest concern (25 per cent).

40. Viewed by sector, access to finance is the most important constraint. It is named as the top concern of 18 per cent of all enterprises in the manufacturing and retail sector and 15 per cent of enterprises in services. For the second-ranking obstacle, the picture is more diverse. For manufacturing, it is access to electricity (16 per cent); for retail, it is informality (13 per cent); and for services, it is the tax rate (12 per cent).

41. Finally, grouping constraints thematically, business regulations (including informality, tax rates, customs and trade regulations, tax administration, business licensing and permits, courts, access to land, and corruption) emerge as the biggest constraint, with almost 50 per cent of enterprises identifying them as such. Infrastructure, which includes access to electricity and transportation, comes second. Access to finance ranks third. Although many constraints are common to all entrepreneurs regardless of their gender, enterprises owned by women may face additional constraints, such as discriminatory policies and laws, including not being able to open their own bank account, sign a contract or hold land titles.²

² Almost 90 per cent of all 143 countries covered by a recent study had at least one legal difference restricting women-owned enterprises; see World Bank: *Women, business and the law 2014: Removing restrictions to enhance gender equality* (London, 2013).

Figure 3.2. Constraints grouped thematically



Source: IFC (2013), op. cit.

42. The findings of the ILO's enterprise surveys conducted in over 30 countries as part of its work on an enabling environment for sustainable enterprises (ESEE)³ confirm that business regulations, access to finance, skills and lifelong learning, and infrastructure are among the top five challenges faced by SMEs.

3.2. Problems and disadvantages faced by workers in SMEs

43. It is often assumed that SMEs provide jobs that are of lower quality than those in larger enterprises. There is considerable evidence in support of this view, although much of the data and research is related to developed countries, particularly the EU.⁴ Substantial progress has been made on the operational definition of the quality of employment. Since 2000, the ILO, in cooperation with the United Nations Economic Commission for Europe and Eurostat, has been developing definitions and computation guidelines for quality of employment indicators. The Expert Group on Measuring Quality of Employment has devised a statistical framework for measuring the qualitative dimension of employment, which distinguishes seven dimensions of the quality of

³ For details on the enabling environment for sustainable enterprises, see section 5.3.

⁴ Brendan et al.: "The quality of employment and decent work: Definitions, methodologies, and ongoing debates", in *Cambridge Journal of Economics*, 2013.

employment (see figure 3.3). The framework is based on the ILO manual on defining and using decent work indicators.⁵

Figure 3.3. Dimensions of the quality of employment



Source: Expert Group on Measuring Quality of Employment: *The Statistical Framework for Measuring Quality of Employment*, unpublished (2012).

44. A study into the quantitative and the qualitative aspects of employment creation of SMEs in the EU comes to the conclusion that differences in the quality of employment are much more apparent between countries and economic sectors than between enterprises of different size classes.⁶ This is supported by a more recent study into sectoral differences in employment quality in the EU. This study covers four dimensions of employment quality: earnings; prospects (for example, job security and career progression); intrinsic job quality (for example, social and physical environment, work intensity); and quality of working times. The study reports high scores for the chemical industry, utilities, financial services, real estate, and legal and accounting services. Sectors that receive a relatively low score are administrative services, the agro-food industry, food and beverage services, textiles and clothing, transport and storage, and construction. Workers in sectors with poor employment quality are twice as likely to report negative outcomes for health and well-being. Similarly, they are about half as likely to report that they are still able to do their job when they are 60.⁷

45. Nevertheless, SMEs score lower for most aspects of employment quality when compared to larger enterprises (see table 3). Data on **wages** in SMEs in European

⁵ ILO: *Decent work indicators: Concepts and definitions*, Geneva, 2012.

⁶ De Kok et al. (2011), op. cit.

⁷ European Foundation for the Improvement of Living and Working Conditions (Eurofound): *Working conditions and job quality: Comparing sectors in Europe*, Dublin, 2014.

countries reveal that they are between 20 and 30 per cent lower than the national average. There are similar findings for the United States and Japan.

Table 3. Indicators of employment quality: Comparisons between SMEs and LSEs in the EU

Area	Indicator	Size class with highest score
Remuneration	Wage levels	LSE ¹
	Use of performance-related pay schemes	SME
Job flexibility	Level of overtime	LSE
	Level of part-time work	SME
	Flexitime arrangements	LSE
Job security ²	Employing from temporary work agencies	SME
	Use of fixed-term contracts	SME
	Job losses due to death of enterprise	LSE
Employee participation	Coverage by collective labour agreements	– ³
	Employee representation	LSE
Skills development	Use of training and development activities	LSE

¹ LSE = large-scale enterprises. ² The three indicators on job security assume an inverse relationship between the score and the quality of employment: the higher the employment from temporary work agencies, the lower the employment quality and vice versa.

³ Cannot be determined based on the available data.

Source: De Kok et al. (2011). The data of the enterprise surveys used only cover areas of job quality emerging from the contractual relationship between employers and workers. They do not cover areas of work quality such as the physical conditions of work or the risk of accidents.

46. The limited research that is available on **social protection** in SMEs suggests that there are shortcomings in the provision of social security to workers of SMEs in low- and middle-income countries. In some of these countries, enterprises with less than a certain number of employees are exempted from obligatory contributions to and coverage by social security. For example, in India and Nigeria, workers in enterprises with fewer than ten employees are not covered by health and other social insurance schemes. ⁸ However, in a number of countries, including Brazil, China, Jordan, Lesotho, Mongolia, Rwanda, South Africa and Thailand, measures to extend social protection coverage through non-contributory and contributory systems have enhanced social protection coverage for large groups of the population, including workers in SMEs. ⁹ For SME workers in many countries, the most significant determinant for access to social security provisions remains whether they are employed in the formal or the informal economy. ¹⁰

⁸ ILO: *Can productivity in SMEs be increased by investing in workers' health? Taking stock of findings on health protection of workers in small and medium-sized enterprises and their impacts on productivity* (Geneva, 2014).

⁹ ILO: *Social security for social justice and a fair globalization*, Report VI, International Labour Conference, 100th Session, Geneva, 2011; ILO: *World Social Protection Report 2014/15: Building economic recovery, inclusive development and social justice* (Geneva, 2014).

¹⁰ ILO: *Can productivity in SMEs be increased by investing in workers' health?*, op. cit.

47. As for **working hours**, there is no clear pattern across countries. In certain countries, such as Japan, working hours are lower in smaller enterprises, while in others, such as Brazil, India, United States and some EU countries, they are higher.¹¹

48. In countries outside Europe, **job tenure** seems to be significantly longer in larger enterprises, indicating higher job security. In the United States, workers in businesses with fewer than 25 employees have job tenures that are half the length of those of workers in enterprises with 25 or more employees. Similar trends are reported from Japan and Brazil. One possible explanation, besides the higher entry and exit rates of SMEs, is that career development is difficult in SMEs. Therefore, workers are more likely to move to larger companies, after gaining some skills and experience in smaller enterprises.

49. **Human resource management (HRM) practices** are less present and developed in SMEs, but there is a considerable number of SMEs applying innovative HRM practices. In Germany, high-performance work systems are found in 11 per cent of enterprises of up to 19 employees and in a third of those with 20–199 employees.¹² In Italy, 35 per cent of small enterprises have fairly developed HRM systems and 22 per cent combine innovative HRM practices with well-established industrial relations systems.¹³ European SMEs are characterized by significant initiatives in training and skills development, with 30 per cent of SMEs carrying out continuous vocational training. In Japan, 47 per cent of SMEs (of between 30 and 99 employees) introduced performance-related pay, 26 per cent had performance evaluation systems, and 66 per cent provided both off-the-job and systematic on-the-job training.

50. **Industrial relations** and collective bargaining have an important role to play in improving employment security and working conditions. Therefore, the ILO recommends that SMEs and their workers should be encouraged to ensure that they are adequately represented, in full respect of freedom of association.¹⁴ However, industrial relations are still weak in SMEs, and both trade union membership and company-level collective bargaining are low. Some research exists on strategies for closing the gap in representation in micro and small enterprises. This reveals that organizing workers in SMEs requires trade unions to take a differentiated approach in order to cater for the interests of workers in SMEs that differ from those of their traditional members.¹⁵ Union density in SMEs is estimated at 2 per cent in France, 15 per cent in the Netherlands, 13 per cent in Ireland and less than 2 per cent in Japan. The situation with respect to employers' associations is more diverse. In Austria, Finland, France, Italy, Netherlands and Spain, both employer representation and collective bargaining coverage in SMEs are a significant part of national industrial relations systems. In the United Kingdom, collective bargaining takes place in only 4 per cent of SMEs. In the United States, both union density and collective bargaining coverage are low.

51. **Occupational safety and health (OSH)**, or the lack thereof, has both macroeconomic and microeconomic effects. The ILO estimates that, globally,

¹¹ For this and the following three sections, see Eurofound: *Industrial relations in the EU, Japan, US and other global economies, 2005–2006* (Dublin, 2007).

¹² P. Edwards and M. Ram: "Surviving on the margins of the economy: Working relationships in small, low-wage firms", in *Journal of Management Studies* (2006, Vol. 43-4).

¹³ L. Bordogna and R. Pedersini: *Between the "black hole" and innovative labor relations and HRM practices in small size enterprises: The Italian experience of late '90s in comparative perspective*, unpublished (2001).

¹⁴ See the Job Creation in Small and Medium-Sized Enterprises Recommendation, 1998 (No. 189).

¹⁵ Global Labour University: *Strategies for closing the representation gap in micro and small enterprises*, 2010.

occupational accidents and work-related diseases cause over 2.3 million avoidable deaths annually¹⁶ and that their economic costs amount to around 4 per cent of the world's GDP.¹⁷ Research finds that the work environment is more hazardous in small enterprises than in large ones. In Europe, 82 per cent of all occupational injuries and 90 per cent of all fatal accidents occur in SMEs.¹⁸ However, the incidence rates for work accidents declined from over 4,000 days lost per hundred thousand employees in 1996 to fewer than 3,000 days in 2007.¹⁹

52. **Job satisfaction** tends to be higher for employees of SMEs. This may be related to factors such as greater work autonomy and a lower degree of division of labour. Employees also value the personal relationships with management in SMEs. Another reason proposed is the fact that SMEs offer a more stable working environment in the sense that strategies change less often and reorganizations, mergers and takeovers occur less frequently than in large enterprises.²⁰

53. In summary, although much has been learned, there is still a sizeable knowledge gap concerning the quality of employment in SMEs. No solid data are available on the quality of SME jobs in low- and middle-income countries. Based on the evidence from the EU, SMEs generally score lower for the quality of employment than larger enterprises. This is not surprising, as SMEs pay lower wages and offer fewer fringe benefits because of their comparatively lower productivity. However, in view of the large contribution SMEs make to employment, including the fact that they very often employ priority groups such as young people, older workers and less-skilled workers, it would be inappropriate to consider reducing or abandoning the support for this sector. Instead, the challenge is to support SMEs in increasing their productivity and growth, while at the same time improving the quality of jobs. Guaranteeing fundamental principles and rights at work at all times would be an important first step, but this remains a major challenge, particularly in the large number of SMEs in the informal economy and in agriculture.²¹

54. Another important finding of this section is that the economic sector in which an SME operates has a stronger influence on the quality of employment than the size of the enterprise. Therefore, when policy-makers design future interventions to improve the quality of employment, it might be more effective to focus on specific sectors rather than on size segments.

¹⁶ ILO introductory report for the 2014 World Congress on Safety and Health at Work (Frankfurt am Main, August 2014). The calculations are based on 2010 occupational injury data from selected ILO member States and 2011 data from the World Health Organization on the global burden of disease.

¹⁷ International Labour Office and World Day for Safety and Health at Work (2003).

¹⁸ European Agency for Safety and Health at Work: *Occupational safety and health and economic performance in small and medium-sized enterprises: A review* (2009).

¹⁹ Eurofound: *Health and safety at work in SMEs: Strategies for employee information and consultation* (2010).

²⁰ De Kok et al. (2011), op. cit.

²¹ ILO: *Fundamental principles and rights at work: From commitment to action*, Report VI, International Labour Conference, 101st Session, Geneva, 2012.

Chapter 4

SME policies: Definition, rationale and linkages with other policy areas

55. This chapter provides contextual information on SME policies by defining the subject matter, their rationale and linkages to other relevant policies that are important for SMEs and their contribution to employment but do not specifically target them.

4.1. Definition and objectives

56. In the context of this report, SME policies are defined as public initiatives designed to promote existing enterprises below a certain size.¹ SME policies may target enterprises directly or indirectly. Examples of direct SME policies are financial and non-financial support services, and the integration of SMEs into larger networks of producers or value chains. Indirect support is very often provided through interventions aiming to improve the enabling environment for SMEs, such as simplified registration requirements or tax regimes, or differential labour regulations. The instruments most commonly used in SME policies are credit, grants, technical assistance and fiscal incentives.² SME programmes are considered to be an integral part of policies, in that they make an intervention operational by means of a plan of action to accomplish a specific goal. Targeting SMEs is not considered to be an end in itself, but a means to creating growth, quality employment and shared prosperity.

57. Entrepreneurship policies are closely related to SME policies and in practice are often combined with them. The key difference is that entrepreneurship policies target individuals rather than existing enterprises. Their primary objective is to encourage more people to consider entrepreneurship as an option and to support the pre-start, start-up and early post-start-up phases of the entrepreneurial processes.³ Entrepreneurship policies are very often designed and delivered to enhance the motivation and skills of individuals and the opportunities available to them.⁴ There are clear synergies between entrepreneurship policies and SME policies, especially in the establishment of an

¹ P. Ibararán, A. Maffioli and R. Stucchi: *SME policy and firms' productivity in Latin America*, IZA Discussion Paper No. 4486 (Institute for the Study of Labor (IZA), 2009); Independent Evaluation Group: *The big business of small enterprises: Evaluation of the World Bank Group experience with targeted support to small and medium-size businesses 2006–12* (Washington, DC, 2014).

² Ibararán et al., op. cit.

³ See A. Lundstrom and L.A. Stevenson: *Entrepreneurship policy: Theory and practice* (New York, Philadelphia, 2005).

⁴ A key ILO product is the entrepreneurship education package for secondary schools, Know About your Business, with 2.3 million participants over the last decade; see S. Asad and V. Rose-Losada: *Know About Business 2013: An outreach report from the ILO's entrepreneurship education programme* (Geneva, ILO, 2013).

enabling environment, access to finance and management skills. The ILO therefore recommends that both types of policies should be designed as a package.

4.2. Rationale

58. There are two main economic justifications for SME policies.⁵ One rationale is the existence of market failures that might hinder SMEs' performance and their participation in market activity, leading to lower growth and employment. SME policies address these market failures, such as incomplete information, the lack of availability and high cost of certain services, or public goods problems. Frequently cited examples are:

- a lack of access to finance because of the inability of banks to assess the risks of lending to SMEs;
- a lack of information among SMEs on the benefits of certain support services, such as training or consultancy;
- a lack of providers for certain services, or providers' unwillingness to scale down their services to meet the demand of smaller enterprises because of an unfavourable ratio of fixed costs to revenues; and
- enterprises' reluctance to invest in research and development because they fear free knowledge spillovers to other enterprises.

59. The second rationale for SME policies is that this size class makes special contributions to economic development and poverty alleviation and therefore merits support. Arguments frequently brought forward to justify targeted support to SMEs are their contribution to employment generation because of their higher labour intensity and their positive impact on efficiency, innovation and productivity through enhanced competition.

60. The economic literature is clear that neither a market failure nor SMEs' special contribution to development goals is sufficient to warrant government intervention; an intervention is justified only when it leads to net welfare gains.⁶

61. There are also several sceptical views that question the rationale for SME policies. These range from a traditional non-interventionist position that calls for policies that do not favour enterprises of any size (except for those with specific social objectives such as assisting very poor entrepreneurs) to views that stress the importance of systemic, non-targeted reforms, such as a reliable infrastructure, good governance of the public sector, political stability, a sound enabling environment for business and an adequately educated workforce.⁷ Sceptics also argue that SME policies are usually too insignificant to make any global difference and that such interventions can be justified only if sustainable local markets for SME support services are built up or if governments embed the interventions in national programmes.

62. The debate on whether or not to adopt SME policies has not yet been resolved. There is broad agreement that market failures do exist⁸ and that there is a need to overcome them through SME policies, but there is no agreement that SMEs make special

⁵ See, for example, Ibararán et al., op. cit.

⁶ D.J. Storey: *Entrepreneurship and SME policy*, unpublished, 2008.

⁷ Independent Evaluation Group, op. cit.

⁸ See, for example, D.J. Storey: "Evaluating SME policies and programmes: Technical and political dimensions", in M. Casson et al. (eds): *The Oxford Handbook of Entrepreneurship* (Oxford, 2006).

economic contributions.⁹ The best way to reach consensus is to overcome the lack of reliable quantitative impact evaluations and to track the results of SME policies, compare their cost with the associated economic and social benefits, and assess their effectiveness compared with other interventions that do not target enterprises below a certain size. There is vast agreement that SME policies need to be firmly rooted in a clear theory of change and evidence-based assessments of results.¹⁰ Promoting an evaluation culture is also important in view of the fact that governments, non-governmental organizations and donors continue to spend considerable budgets on SME policies.¹¹

4.3. Linkages with other key policy areas

63. This report focuses on analysing the effectiveness of SME policies, which are defined as policies targeted at enterprises below a certain size. It is understood that a range of other economic policies may also have a substantial impact on SMEs, may be a precondition for sustainable SME development or may disproportionately benefit SMEs. However, these other policies are not the focus of this report, since they do not specifically target one size class of enterprises to the exclusion of others and they have, in any case, already been discussed extensively by constituents in recent years. Nevertheless, some broader policies and their relevance for SMEs are briefly set out below in order to underline their importance and to promote coherent analyses and approaches.

64. **Macroeconomic policies** are among the most important factors for the development of enterprises of any size.¹² Monetary, financial, fiscal and exchange rate policies not only directly influence the cost of credit and other inputs of enterprises, but also impact on aggregate demand. SME policies will only work if they are underpinned by a supportive macroeconomic policy framework that promotes productivity growth, domestic and foreign demand and economic stability.

65. **Investment and physical infrastructure policies** can play an important role in overcoming one of the biggest challenges reported by enterprises, namely the lack of adequate infrastructure. By using employment-intensive methods, they can also contribute to poverty eradication through the jobs they create. And if the related programmes use locally available inputs to the greatest possible extent (as practised by the ILO), SMEs can also benefit as direct suppliers.¹³

⁹ See, for example, Independent Evaluation Group, *op. cit.*

¹⁰ See, for example, OECD: *OECD framework for the evaluation of SME and entrepreneurship policies and programmes* (Paris, 2007).

¹¹ The Consultative Group to Assist the Poor (CGAP) estimates that, as at 2011, public development finance institutions allocated US\$25 billion of funding to SMEs and that the Official Development Assistance (ODA) for SMEs amounted to \$1 billion in 2009 (total ODA was \$120 billion in 2009 according to the OECD). A recent evaluation of the World Bank Group's targeted support to SMEs shows that these interventions amounted to \$18 billion of commitments, expenditures and exposure from 2006 to 2012, comprising 16 per cent of the IFC's total portfolio value, 21 per cent of the Multilateral Investment Guarantee Agency's gross exposure and 2 per cent of the World Bank's investment commitments; see Independent Evaluation Group, *op. cit.*

¹² For the ILO's approach to pro-employment macroeconomics see also ILO: *Employment policies for sustainable recovery and development*, Report VI, International Labour Conference, 103rd Session, Geneva, 2014.

¹³ One of the ILO's largest technical cooperation programmes is the Employment-Intensive Investment Programme with a portfolio of US\$120 million operating in 45 member States: see *ibid.*

66. **Industrial policy** has seen a strong revival in recent years. It comprises the efforts of government to promote a specific sector or cluster that is expected to accelerate the process of structural transformation, leading to better prospects of inclusive growth.¹⁴ Depending on the number of SMEs in the sectors or clusters chosen, industrial policies can be very important for SMEs. Policies targeting SMEs are a good complement to industrial policies if they help SMEs to acquire the skills and competences required for sustained diversification and productive transformation.

67. As noted in Chapter 3, the mismatch between the skills of the workforce and the demand of enterprises is a significant constraint reported by enterprises. **Skills development policies** covering basic education, initial training and lifelong learning play an important part in addressing this skills mismatch. These policies are crucial to increasing the productivity of enterprises of any size, including SMEs, which is, in turn, a key requirement for creating more and better jobs.¹⁵

¹⁴ See J.M. Salazar-Xirinachs, I. Nübler and R. Kozul-Wright (eds): *Transforming economies: Making industrial policy work for growth, jobs and development* (Geneva, 2014).

¹⁵ See ILO: *Skills for improved productivity, employment growth and development*, Report V, International Labour Conference, 97th Session, Geneva, 2008; and ILO: *A skilled workforce for strong, sustainable and balanced growth: A G20 training strategy* (Geneva, 2010).

Chapter 5

Relevance and effectiveness of SME policies in supporting ILO priorities

5.1. Introduction

68. This chapter summarizes the recent empirical evidence on the effectiveness of SME policies, and analyses the extent to which SME policies can help to achieve ILO priorities. The focus is on the most important interventions in terms of the demand from ILO member States and the outreach to beneficiaries. These are:

- enhancing access to finance and entrepreneurship training;¹
- establishing an enabling environment for enterprises;
- formalizing enterprises in the informal economy;
- promoting SME productivity and improving working conditions; and
- creating value chain interventions.

The chapter concludes with an update on new trends in SME policies.

69. For each of the interventions listed above, the chapter: (1) briefly presents the model of change that shows how the intervention is supposed to contribute to the intended changes; (2) summarizes the global evidence of whether the model of change works; and (3) documents what is known about the impact of ILO interventions in the particular area.

70. When documenting the global evidence and the ILO's evidence on the effectiveness of SME policies, the chapter focuses on rigorous impact assessments that estimate the causal impact of an intervention. Priority is given to experimental or quasi-experimental methodologies.² The use of such designs allows counterfactuals to be estimated: that is, what would have happened without the intervention. Alternatively, non-experimental econometric studies, based on statistical analysis of economic relations, are used. This method also helps to quantify effects, but it is difficult to infer causal relationships. The focus on quantitative evaluation approaches is important for two reasons. First, there is a general lack of quantitative impact assessments of SME policies.

¹ As these interventions are often offered as a package, they will be dealt with together.

² An experiment tests an SME intervention, such as a training or microfinance programme, by randomly assigning businesses to treatments or to a control group representing the status quo. This approach reduces the likelihood of systematic differences between treatment and control group that might affect the measured outcome and helps to credibly attribute observed positive or negative effects to the intervention. Quasi-experiments use methods other than random assignment to construct treatment and control groups. Possible differences in the groups may reduce the credibility of results.

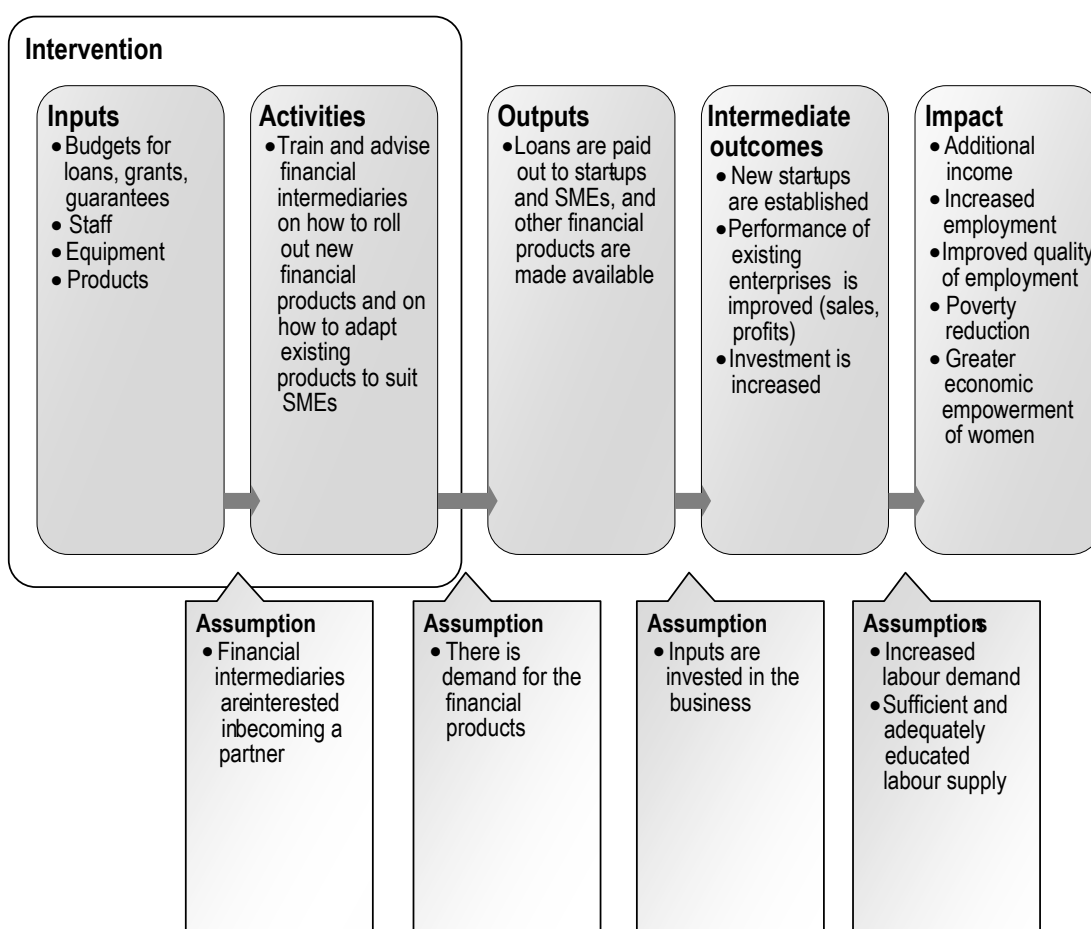
Second, less rigorous methods tend to overestimate policy impact. If no rigorous evidence exists, this will be clearly indicated.

5.2. Access to finance and entrepreneurship training

Intervention logic

71. As shown in the previous chapter, SMEs often have constrained access to finance. Therefore, many interventions are designed to provide them with access to financial services such as loans, guarantees, grants, savings products, insurance or leasing facilities. Frequently, the interventions not only aim to provide SMEs with access to these services, which very often were not available to them before, but also attempt to lower the cost of the services. Figure 5.1 provides an overview of the logic of this type of intervention.³ Access to finance is expected to provide the financial inputs needed to maintain and expand an enterprise's operations. This should contribute to an improvement in the performance of SMEs, resulting in higher sales and profits, and ultimately leading to increased labour demand, and higher income and employment generation.

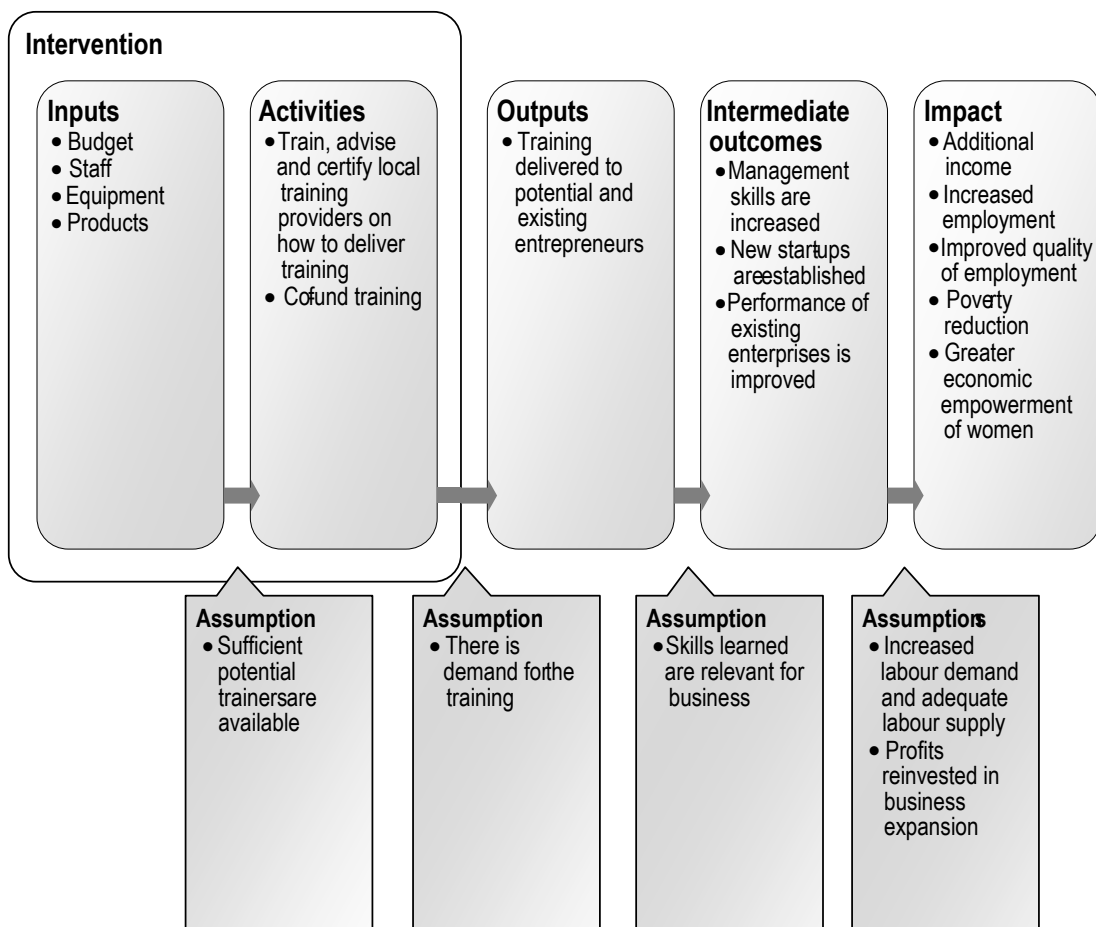
Figure 5.1. From projects to impact: Intervention model for access to finance



³ The intervention models are based on M. Grimm and A.L. Paffhausen: *Interventions for employment creation in micro, small and medium sized enterprises in low and middle income countries – A systematic review*, unpublished, 2014; and N. Fiala and M. Pilgrim: *Intervention models and performance indicators of the ILO Small Enterprises Unit* (Berlin, Geneva, 2013).

72. Entrepreneurship training refers to all types of training which teach the skills to start a new enterprise or to improve the core management and administrative functions of existing enterprises. This includes special programmes for women entrepreneurs, which may provide additional content on gender. Figure 5.2 sets out the intervention model for entrepreneurship and management training programmes. The measure is expected to improve the management skills of potential and existing entrepreneurs who are either expected to start a business or expand their existing business as a result of the training. Based on their newly acquired skills, beneficiaries are expected to improve the performance of their enterprises, leading to an increased demand for labour and additional income and employment generation.

Figure 5.2. From projects to impact: Intervention model for entrepreneurship training



Summarizing the global evidence

73. For developing countries, the **global evidence on the impact of entrepreneurship training and access to finance** can be summarized as follows.⁴ Of the training interventions that were assessed, 40 per cent showed significant positive effects on

⁴ This section mainly relies on two recent systematic reviews assessing the impact of SME policies in developing countries. Grimm and Paffhausen, op. cit., cover 54 studies that qualify as rigorous assessments. Y. Cho and M. Honorati: *Entrepreneurship programs in developing countries: A meta regression analysis*, Social Protection and Labor Discussion Paper No. 1302 (World Bank, Washington, DC, 2013) includes a sample of 37 studies. Grimm and Paffhausen focus on employment effects and do not systematically review income effects. Cho and Honorati also cover income effects and show that 28 per cent of all interventions (training, finance or both) show significant results with regard to income.

employment, while the remaining 60 per cent did not. Where there were significant effects, these were considerable. A third of the interventions produced medium-sized or large effects, 45 per cent had small effects and 22 per cent produced negative effects.⁵

74. Of the interventions providing access to finance, 35 per cent showed significant positive effects on employment. The magnitude of these effects was, however, mostly small. Only 18 per cent of the interventions with a significant effect had a medium-sized or large effect.⁶ One possible explanation is that the majority of these interventions were microcredit schemes offering loans of between US\$100 and \$2,000, which were typically used as working capital and not for long-term investments into equipment or buildings that might lead to business expansion and increased employment. There are only a few assessments of grant schemes and no studies on the employment effects of microinsurance products.

75. The global evidence also suggests that for both types of interventions, programme success in terms of employment creation can be further increased if the intervention incorporates one or more of the following features:

- (a) Combining entrepreneurship training with access to finance works better than stand-alone interventions. There is a strong case for partnering with microfinance institutions when implementing programmes, since the ability to obtain a loan may provide entrepreneurs with an incentive to apply the new business practices that they learn from training programmes.
- (b) Programmes for young people are more likely to have positive results. One possible explanation is that there is a greater shortage of entrepreneurial skills in this age group than in other age groups. Therefore, the relative impact of these interventions is higher. Another reason might be that the willingness to establish a new enterprise is more prevalent in younger age groups. A consistent finding of the surveys of the Global Entrepreneurship Monitor has been that, regardless of the level of national development, the highest percentage of early-stage entrepreneurs is found in the 25–34 age group.⁷
- (c) Programmes targeting women appear to be less successful in terms of income generation and employment creation. However, this should not be used as an argument to stop these interventions, since the results probably reflect the different goals of women entrepreneurs and the structural inequities they face. The latter often include women's lack of decision-making autonomy within the family, the additional requirements on their time and limited educational opportunities. Nevertheless, the findings do call for a rethinking of current approaches, especially on the need to overcome structural inequalities. The most recent evaluation results show that adding new design features to women's entrepreneurship programmes,

⁵ Systematic reviews very often use the so-called standardized effects size reflecting the size of the effect on the treatment compared to the control group as a proportion of its standard deviation. This method makes it possible to compare studies that measure different employment effects, whether it is a probability difference, a percentage growth, or changes in levels. The average standardized effect size of both reviews mentioned above is approx. 0.2 for employment, meaning that the interventions increased employment on average by 0.2 standard deviations. If the standard deviation in the baseline was four workers, it means that employment increased by 0.8 workers. For the classification of small, medium and large effect sizes, see J. Cohen: *Statistical power analysis for the behavioural sciences*, second edition, 1988.

⁶ Grimm and Paffhausen, op. cit.

⁷ See, for example, J.E. Amorós and N. Bosma: *Global Entrepreneurship Monitor: 2013 Global Report* (2014).

such as mobile money services or in-kind capital, increases the decision-making autonomy of female entrepreneurs and improves business performance.⁸

- (d) Programmes delivered by non-state intermediaries tend to perform better. One possible explanation is that these organizations are more familiar with the target groups. Non-state intermediaries also include employers' organizations as well as other business membership organizations which frequently offer non-financial business support services to SMEs. The available results do not allow conclusions to be drawn on the performance of this group of intermediaries.
 - (e) The point in time when evaluations are conducted has an effect on the results. Outcomes measured one to two years after the end of an intervention are more likely to show positive results than those measured a few months after programme completion.
76. Finally, a few observations should be made on how to interpret the results:
- (a) If we take the performance of active labour market policies in OECD countries as a benchmark (39 per cent of which produce significant positive results),⁹ entrepreneurship development interventions in developing countries perform at a comparable level. These interventions can contribute to employment creation with substantial welfare gains.¹⁰
 - (b) Nevertheless, the majority of the studies do not show positive effects on employment. That does not mean, however, that there are no results at all. A large number of studies show that interventions lead to improved business practices (in the case of training initiatives) or income stabilization (for measures promoting access to finance). Fewer studies show improvements in sales or profits and even fewer still show significant effects on employment. The overall pattern is that the further along the results chains from the intervention to the final impact, the more difficult it becomes to show significant results. It is not clear whether this is due to a lack of effectiveness of the interventions or whether evaluation studies do not leave enough time between the end of the intervention and the measurement of employment effects. Frequently, such effects are measured a few months or, at most, two years after the intervention. There are no programmes that track effects two to four years after the intervention.¹¹ It is thus possible that there are positive employment effects that will become apparent over a longer assessment period.
 - (c) The majority of the interventions assessed are aimed at micro-enterprises or self-employed people, which reflects a desire to target high-need populations that are excluded from financial or non-financial services. These programmes should be maintained, as they make valuable contributions to increasing income and income security and can also produce effects on employment. From the standpoint of additional employment creation, also targeting young, fast-growing enterprises

⁸ M. Buvinic and R. Furst-Nichols: *Promoting women's economic empowerment: What works?*, World Bank Group Policy Research Paper No. 7087 (2014).

⁹ D. Card, J. Kluve and A. Weber: "Active labor market policy evaluations: A meta-analysis", in *Economic Journal* (2010, Vol. 120). It should be noted that active labour market policies generally include entrepreneurship training, but also include measures such as job search assistance or cover public sector jobs that do not fall under the category of SME policies.

¹⁰ Cho and Honorati, op. cit.

¹¹ Evaluations of active labour market policies in OECD countries clearly show that the long-term employment effects (three years after intervention) are stronger than the short- or medium-term results; see Card et al. (2010), op. cit.

should be considered, since it is this subgroup of the SME sector that generates most of the new jobs (see Chapter 2). It should be noted, however, that there is as yet an insufficient number of impact studies to definitively confirm the hypothesis that high-growth enterprises will benefit more from interventions.

- (d) The quality of the training is not a variable in the assessments.¹² The underlying assumption is that interventions are delivered at a consistent quality, which is unlikely. It would be better to find appropriate indicators for the quality of training and to assess whether quality influences programme success.
- (e) In most of the experiments, training is offered free of charge, whereas some ILO programmes charge fees to participants in order to improve the programmes' financial sustainability as well as to filter out uncommitted participants. Charging fees might have a positive impact, under the assumption that it helps to ensure the selection of more committed participants. This still has to be proven in the case of training. In the case of access to finance, it is widely acknowledged that charging interest rates or fees is a good practice in order to establish sustainable programmes.
- (f) The advantage of systematic reviews when compared to impact assessments of individual interventions is that they can help to identify design factors across countries and regions that have an influence on the impact. In this context, the two recent systematic reviews on the effectiveness of SME interventions in developing countries have contributed to reducing the heterogeneity of earlier studies that could not detect clear trends.¹³ However, the sample size of these systematic reviews is still limited. More stocktaking exercises and systematic reviews are needed. These should also include cost–benefit analyses, as, currently, almost none of the assessments have data on cost-effectiveness that compare the benefits with the cost of interventions.
- (g) With regard to the quality of jobs created, it is clear that interventions can contribute to generating additional income, which is a key dimension of employment quality. However, there is a lack of evidence beyond the level of income generation. Future impact assessments should cover other important areas of working conditions.

77. One of the **key policy implications** is that interventions promoting entrepreneurship development through financial and non-financial support services can contribute to the creation of more and better jobs. Furthermore, providing packages that combine access to finance with non-financial services works better than stand-alone interventions, which are still a frequent practice and should be reduced. The effects on employment are higher for young people as compared to the general population. This leads to the conclusion that entrepreneurship development for young people should continue to be one of several active labour market policies directed at combating youth unemployment and underemployment. Furthermore, there may be a need to adapt interventions targeting women entrepreneurs. One solution to be tested is to include additional content on women's economic empowerment to better address the specific constraints they face.

¹² Except for Cho and Honorati, op. cit., who take the delivery model (state or non-state provider) as a quality proxy, which is probably not sufficient.

¹³ D. McKenzie and C. Woodruff: *What are we learning from business training and entrepreneurship evaluations around the developing world?*, Policy Research Working Paper 6202, unpublished, 2012.

Impact of ILO interventions

78. As the ILO is running some large-scale pro-SME interventions, especially in the area of entrepreneurship training and access to finance,¹⁴ it is important to evaluate whether these programmes produce the intended effects. As can be seen in table 4 below, eight impact assessments testing ILO interventions have been published so far.¹⁵ These studies were either conducted by the ILO in cooperation with external researchers or only by external researchers who chose ILO products because of their prevalence in the local market.

Table 4. Effectiveness of interventions using ILO products for entrepreneurship training and access to finance

Type of intervention	Statistically significant effects on: ¹		
	Business practices	Income	Employment
Uganda: combining entrepreneurship training based on the ILO's Start and Improve Your Business programme with loans or grants	+	+(for loans and training: 54 per cent increase in profits)	+(for loans and training: employment increases between 45 per cent and 66 per cent)
Viet Nam: providing gender and business management training based on the ILO's Get Ahead programme, in combination with microloans	+	+	Not measured
Ghana: business management training based on the ILO's Improve Your Business programme as an award for participating in a business plan competition	Not measured	0	0
Sri Lanka: combining entrepreneurship training based on the ILO's Start and Improve Your Business programme with grants for existing and potential women-owned micro-enterprises	+	+	0
Pakistan: business training based on the ILO's Know About Business programme and loans for rural microfinance clients	+	+	0
Ghana: management training for existing SMEs based on the ILO's Start and Improve Your Business programme	+	+	Not measured
Tajikistan: training and loans for potential women-owned start-ups based on the ILO's Get Ahead programme	+	+	+(for loans and training: self-employment increases by 60 per cent)

¹⁴ In terms of outreach, the largest ILO training programme is the entrepreneurship training package Start and Improve Your Business, with 4.5 million participants (2003–10); see S. Lieshout, M. Sievers and M. Aliyev: *Start and improve your business: Global tracer study 2011* (Geneva, 2012). Further important training and advisory packages focus on women entrepreneurs and agricultural cooperatives. The largest ILO programme promoting access to finance is the Making Microfinance Work package, which trains financial services providers. To date, 2,700 managers of commercial banks, cooperatives and credit unions have been trained on how to improve access to finance for underserved clients such as SMEs.

¹⁵ As for the global evidence, only studies with an experimental or quasi-experimental design are included. Tracer studies tracking beneficiaries before and after the intervention, such as the global tracer study on the Start and Improve Your Business programme, are not included as they do not have a control group; they nevertheless remain valuable monitoring tools.

Type of intervention	Statistically significant effects on: ¹		
	Business practices	Income	Employment
Philippines: training for clients of a local microfinance institution based on the ILO's Start and Improve Your Business programme	+	+	0

¹ "+" refers to a statistically significant positive effect. "0" means that no effect could be found; there were no cases of a significant negative effect. For detailed results, see the table in the appendix.

79. The sample of impact assessments of ILO interventions is still too small to allow for a systematic review that could identify key design features across interventions that influence programme success. However, the summary of the key findings shows that the conclusions of these assessments are similar to those that have emerged from the global evidence. First of all, the vast majority of programmes were successful in changing business practices and in generating additional income. Only relatively few programmes had significant effects on employment, but some interventions did not measure this indicator. Second, the ILO's experience also confirms the conclusion from the global evidence that interventions on access to finance and to non-financial services should be combined. Third, women entrepreneurs benefited less from ILO interventions in terms of income generation or job creation. Fourth, the majority of interventions targeted micro-enterprises and self-employed people. Fifth, most of the assessments did not include a cost-benefit analysis. Finally, in contrast to the global evidence, the ILO has started to measure the quality of jobs created, beyond the income dimension. The assessments have shown that it is possible, for example, to advance the empowerment of women. However, more assessments need to be conducted.

80. The ILO is broadening the evidence on the effectiveness of pro-SME interventions. There are five new studies in the pipeline which test the long-term effects of entrepreneurship training and access to finance. This demonstrates the ILO's commitment to generating credible evidence on the effectiveness of its interventions.

5.3. Enabling environment

Intervention logic

81. Many SME policies have a component aimed at improving the enabling environment for this segment of enterprises. The key argument brought forward is that there is very limited value in trying to promote SMEs at the enterprise level in an environment that is hostile to them. Unlike large enterprises, SMEs cannot afford to hire specialists to deal with complex rules and regulations. The fact that SMEs are hit harder by an unconducive enabling environment is also often referred to as a lack of a level playing field.

82. The most common definition of an enabling environment is provided by the Donor Committee for Enterprise Development (DCED). (The ILO's own Enabling Environment for Sustainable Enterprises approach adopts a wider definition that includes economic, political, social and environmental conditions.) The DCED defines the business environment as "a complex of policy, legal, institutional, and regulatory conditions that govern business activities. It is a sub-set of the investment climate and includes the administration and enforcement mechanisms established to implement

government policy, as well as the institutional arrangements that influence the way key actors operate.”¹⁶

83. Changing the enabling environment is a complex field of intervention. It consists of various functional areas that affect business activity, including: simplifying business registration and licensing procedures; streamlining tax policies and administration; facilitating access to finance; adapting labour laws and administration; improving the overall quality of regulatory governance; improving land titles, registers and administration; simplifying and accelerating access to commercial courts and to alternative dispute-resolution mechanisms; broadening public–private dialogue processes, including the promotion of social dialogue; and improving access to market information.¹⁷

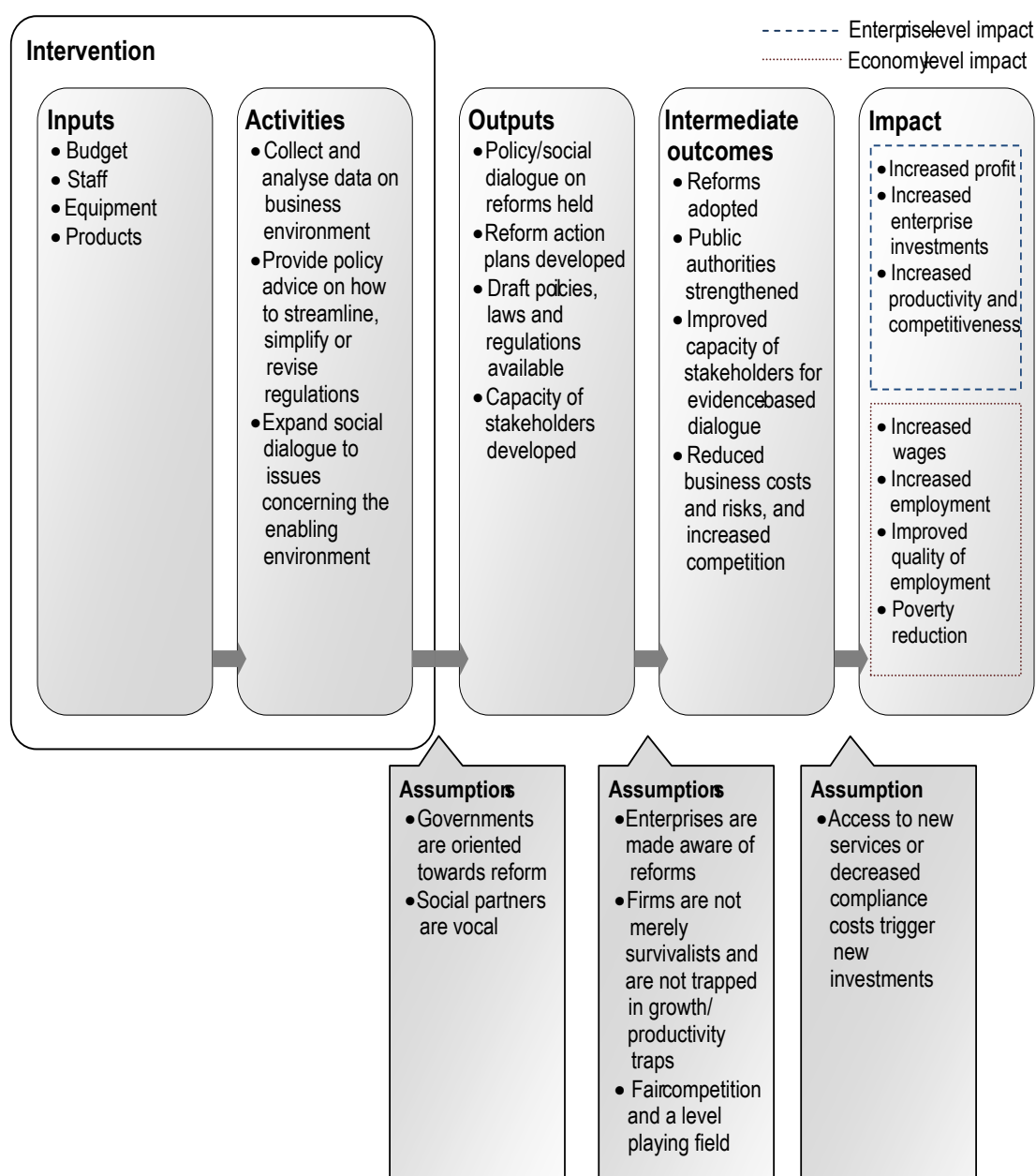
84. The abovementioned interventions often benefit enterprises of any size class, but are frequently justified because of their special importance for SMEs. In addition, some countries offer exemptions or compliance thresholds that are specific to one enterprise size segment. Two widespread examples are tax reductions for SMEs and exemptions from labour legislation; others include special procurement policies and market reservations schemes for SMEs.

85. Figure 5.3 provides an overview of the theory of change linked to enabling environment interventions. Typically, these interventions focus on collecting evidence on whether there is scope to streamline, simplify or revise rules and regulations. This should lead to draft policies, laws and regulations that would improve the enabling environment. Policy dialogue and social dialogue provide the platform to prioritize reforms and identify the most suitable policy options. Once reforms are adopted, they are expected to provide access to new services that will help SMEs to perform better or to reduce their costs of doing business. These decreased compliance costs should also free resources, leading to additional investment and employment generation.

¹⁶ Donor Committee for Enterprise Development (DCED): *Supporting business environment reforms: Practical guidance for development agencies* (2008 edition).

¹⁷ *ibid.*

Figure 5.3. From projects to impact: Intervention model for an enabling environment



Summarizing the global evidence

86. A rigorous measurement of the effects of interventions to promote an enabling environment would ideally be based on a random exposure of some enterprises to the intervention while other similar enterprises remain unexposed. However, it has proven very difficult to apply such experimental evaluation approaches for this area of intervention.¹⁸ Support programmes for improving the business environment are typically implemented at the national level, thereby affecting all SMEs in a country simultaneously.¹⁹ Therefore, the impact of such interventions tends to be measured

¹⁸ The only exception has been business entry reforms such as one-stop shops that have been tested based on experimental impact assessments; for results, see section 5.4.

through cross-country or cross-sectional empirical analysis. This makes it difficult to draw inferences on the causal effect of reforms to an enabling environment.

87. Studies show a significant link between enabling-environment reforms and job creation or economic growth. A recent evaluation of the World Bank Group's SME support programmes shows that an improved enabling environment is significantly associated with employment growth.²⁰ The smaller the enterprises, the larger the effects on employment. Other studies show a clear link between improvements in the enabling environment and economic growth.²¹

88. Apart from these econometric studies, there are other evaluations that examine the impact of enabling-environment interventions in specific functional areas, based on a before and after comparison. These studies estimate the cost reductions achieved or the additional investment realized, without resolving the question of attribution. This makes it difficult to conclude which specific interventions produce the best value for money. The following paragraphs highlight some of the most important findings.

89. In the area of **trade facilitation**, studies focus on estimating the time and costs saved through introducing streamlined or simplified export/import procedures. According to a World Bank analysis, each day gained in accelerating exports increases their total value by 1 per cent.²² A similar study focusing on the Asia-Pacific Economic Cooperation economies estimates that halving the days needed to clear exports could enable an SME to increase its share of exports from 1.6 per cent to 4.5 per cent of total sales.²³ A further quantification by the OECD estimates that, when trade facilitation leads to a reduction in trade transaction costs equivalent to 1 per cent of the value of world trade, aggregate gains of national income amount to approximately US\$40 billion worldwide. All countries would benefit, and non-OECD countries would experience the biggest gains in relative terms.²⁴

90. **Taxes** are also cited as a major constraint for enterprises and can have substantial effects on investment and the entry of new companies. Data on effective first-year and five-year corporate income tax rates for 85 countries show that increases in effective corporate tax rates have a large and significant adverse effect on investment and entrepreneurship.²⁵ Tax compliance costs are significantly higher for smaller enterprises than for larger ones. Data from the EU show that compliance costs for value added tax

¹⁹ See, for example, A. Rahman: *Investment climate reforms and job creation in developing countries: What do we know and what should we do?*, World Bank Group Policy Research Working Paper No. 7025 (2014); or DCED: *Supporting business environment reforms: Practical guidance for development agencies* (2013 edition), Annex: *Measuring donor-supported business environment reform*.

²⁰ The measurements used for an enabling environment were access to finance (captured by whether an enterprise had a bank loan or line of credit), access to electric power (presence of a generator) and reduction of regulatory burden (managers' time spent dealing with public regulations); see Independent Evaluation Group: *The big business of small enterprises: Evaluation of the World Bank Group experience with targeted support to small and medium-size businesses 2006–12* (2014).

²¹ See, for example, World Bank: *Regulation and growth* (2006), covering 135 countries, or E. Bah and L. Fang: *Impact of the business environment on output and productivity in Africa* (2010), covering 30 countries in sub-Saharan Africa.

²² S. Djankov, C. Freund and C.S. Pham: *Trading on time* (2006).

²³ Y. Li and J.S. Wilson: *Trade facilitation and expanding the benefits of trade: Evidence from firm level data* (2009).

²⁴ OECD: "Quantitative assessment of the benefits of trade facilitation", in *Overcoming border bottlenecks: The costs and benefits of trade facilitation* (2009).

²⁵ S. Djankov et al.: "The effect of corporate taxes on investment and entrepreneurship", in *American Economic Journal: Macroeconomics* (2010).

and corporate tax represent only 0.02 per cent of the turnover for large enterprises, but amount to 2.6 per cent of the turnover of small businesses.²⁶ Therefore, tax schemes frequently offer lower rates or exemptions for enterprises below a certain size. An OECD study from 2000 showed that 14 OECD countries had lower corporate tax rates for SMEs, offering reductions of up to 50 per cent.²⁷ Some other countries offer reductions in income and property taxes for a limited number of years or exemptions from registration and transaction taxes. While these tax rebates for SMEs compensate for size-specific disadvantages, they can also create so-called “size traps” that provide disincentives for enterprises to grow beyond a certain threshold.²⁸

91. Tax rebates for SMEs might conflict with the public policy rationale of viewing corporate and other taxes as a source for increasing public revenues in order to fund important investments or expenditures. However, SMEs account for only a small share of tax revenues, and the administrative cost of collecting taxes from smaller enterprises might be higher than the potential additional tax revenue. This trade-off leads to the suggestion that taxes such as value added tax should be levied only on enterprises above a critical size.²⁹ Ultimately, the right balance must be found between an enabling environment for SMEs and the need for governments to find substantial sources of taxation.

92. The view that **labour laws** have a negative impact on economic growth has underpinned much of the policy advice that has been directed at both developing and developed countries. There is, however, a growing body of research that suggests that approaches emphasizing the negative effect of labour laws on employment generation and economic development are simplistic and unsound.³⁰ Labour laws can in fact play an important role in promoting productivity, equity and economic development.³¹ It is necessary to split the vast area of labour laws into specific areas, such as minimum wages, employment protection legislation and industrial relations, in order to obtain meaningful evidence on their impact on economic growth. In fact, the new literature stresses that the effects of labour laws cannot be predicted a priori, through the use of models with universal application. The effects depend on the interaction of legal rules with a number of national, regional and industry-specific conditions and with complementary institutions in capital and product markets.³² There is some literature supporting the need for labour law frameworks to be flexible and adaptive to times of crisis. Many EU Member States, for instance, have made use of short-time working schemes as a means of tackling temporary business problems.³³

²⁶ International Monetary Fund (IMF): *Taxation of small and medium enterprises*, Background paper for the International Tax Dialogue Conference, 2007.

²⁷ D. Chen, F.C. Lee and J.M. Mintz: *Taxation, SMEs and entrepreneurship*, OECD Science, Technology and Industry Working Papers 2002–09 (2002).

²⁸ P. Vandenberg: *The relevance of firm size when reforming the business environment* (2005).

²⁹ IMF (2007), op. cit.

³⁰ J. Berg and D. Kucera (eds): *In defence of labour market institutions: Cultivating justice in the developing world* (Geneva, ILO, 2008).

³¹ G. Davidov and B. Langille (eds): *The idea of labour law* (Oxford, 2011).

³² S. Deakin: *The evidence-based case for labour regulation*, Paper prepared for the Regulating Decent Work Conference, ILO, Geneva, July 2009.

³³ European Labour Law Network: *Protection, involvement and adaptation: European labour law in time of crisis, restructuring and transition* (2010).

93. As in the case of taxation, many countries exempt SMEs from labour legislation. A review of 178 countries found that only 10 per cent of the countries provide a full exemption, while the vast majority give a partial exemption.³⁴ For South Asia, the ILO assessed whether labour-related laws and regulations and exemptions from those laws for enterprises below a certain size affected employment and growth in SMEs.³⁵ Perception-based surveys among 4,600 SMEs in Bangladesh, India, Nepal and Sri Lanka found no positive or negative effects on SME growth. There was also no evidence of so-called size traps, where SMEs do not grow because they want to stay beneath a certain threshold exempting them from certain regulations. The main reasons reported were a lack of awareness about the exemptions or a decision not to comply. Penalties for non-compliance were usually avoided as a result of “under the table” payments.

94. It is often assumed that **land titling** has several positive impacts. However, an experiment in Argentina found that land titling had no effect on access to credit, because the possession of real estate was a necessary but insufficient condition for qualifying for formal credit. Nevertheless, land titling did have substantial positive impacts on housing quality, household size and investment in children’s education. This suggests that allocating solid property rights may reduce poverty in future generations,³⁶ which is consistent with the objectives of reforms to the enabling environment.

95. Some of the abovementioned areas affect **women** disproportionately. One of the main constraints faced by female entrepreneurs is limited access to finance. On average, women have less access than men to basic financial services such as checking and saving accounts as well as to formal credit. Legal and regulatory frameworks may also discriminate against women. In many countries, women do not have equal rights to own property or to obtain employment without their spouse’s permission.³⁷ A recent summary of the evidence on the effectiveness of interventions to promote women’s entrepreneurship development³⁸ could not find any evaluations covering the impact of enabling-environment reforms on enterprises owned by women.

Impact of ILO interventions

96. The ILO has developed its own methodology, the Enabling Environment for Sustainable Enterprises (ESEE), as a basis for providing evidence-based recommendations on how to improve the enabling environment. The methodology analyses political, economic, social and environmental aspects of enterprise development. Since 2011, it has been applied in some 30 countries. As an extension of that methodology, and after a successful pilot in South Africa, the ILO is currently devising its own tool for assessing the cost of excessive bureaucracy for enterprises. In the Free State province of South Africa, compliance costs were estimated at some US\$339 million for the two municipalities studied, with the effect that 32 per cent of enterprises consciously chose to remain informal, while 26 per cent of them chose to limit the number of their own employees. While it is currently too early to report on the

³⁴ J.L. Daza: *Informal economy, undeclared work and labour administration* (Geneva, ILO, 2005).

³⁵ S. White: *Labour laws, the business environment and the growth of micro and small enterprises in South Asia* (ILO, New Delhi, 2014).

³⁶ S. Galiani and E. Scharrogradsky: “Property rights for the poor: Effects of land titling”, in *Journal of Public Economics* (2005, Vol. 94-9).

³⁷ World Bank: *Women, business and the law 2014: Removing restrictions to enhance gender equality* (London, 2013).

³⁸ ILO: *Effectiveness of entrepreneurship development interventions for women entrepreneurs*, ILO–WED Issue Brief (Geneva, 2014).

impacts of reforms, the potential is substantial, if authorities respond to the findings and subsequent advocacy efforts to reduce bureaucracy.

97. The work on the EESE methodology does not yet have a sufficiently long history to permit meaningful impact evaluations. In addition, the impact of this type of intervention is inherently difficult to measure. As a consequence, there are only a few preliminary results emerging from the work under that methodology. In Honduras, reform triggered by the ILO's EESE assessment³⁹ has substantially reduced business registration costs. The Honduran Parliament abolished the mandatory use of notarial services when registering a new enterprise, thereby reducing the cost of registration to approximately one tenth. Extrapolating past annual enterprise registration data linearly into the future, it is estimated that this will lead to a yearly reduction in registration costs of \$5 million and will, in addition, provide an incentive to several thousand businesses in the informal economy to become formal.⁴⁰

5.4. Formalization of informal SMEs

Intervention logic

98. As shown in Chapter 2, the number of informal SMEs is high, especially in developing countries. A high incidence of enterprise informality is associated with several negative developments, such as low productivity, a poor tax base, precarious working conditions and unfair competition. Therefore, there is a strong interest among governments and social partners alike to formalize SMEs. Interventions aimed at the formalization of SMEs are usually considered to be a technical sub-area of the enabling environment because they deal with the regulatory framework conditions that are necessary to ensure the right mix of incentives and sanctions to increase formalization.⁴¹ As this area of intervention is highly relevant for the ILO's broader approach to facilitating the transition from the informal to the formal economy,⁴² it is dealt with as a separate section.

99. Figure 5.4 provides an overview of the intervention model for measures aimed at enterprise formalization. Typically, these interventions focus on simplifying the process for registering informal enterprises and on extending the benefits of formalization. The underlying assumption is that the high cost of registering and running a formal enterprise, as well as the limited benefits derived from formalization, are the main reasons for informality. Consequently, reducing the cost of formalization and extending the benefits should lead to a higher number of registered formal enterprises. A key assumption is that decreased compliance costs would free resources that could then be used for additional investment, employment generation and improved working conditions. An additional argument often brought forward is that since only formal enterprises gain access to public business support services, formal banking and subsidies for product and process

³⁹ ILO, Honduran Council of Private Enterprise (COHEP): *Evaluación del entorno para empresas sostenibles: Honduras 2013* [Assessment of the environment for sustainable enterprises] (Geneva, ILO, 2013).

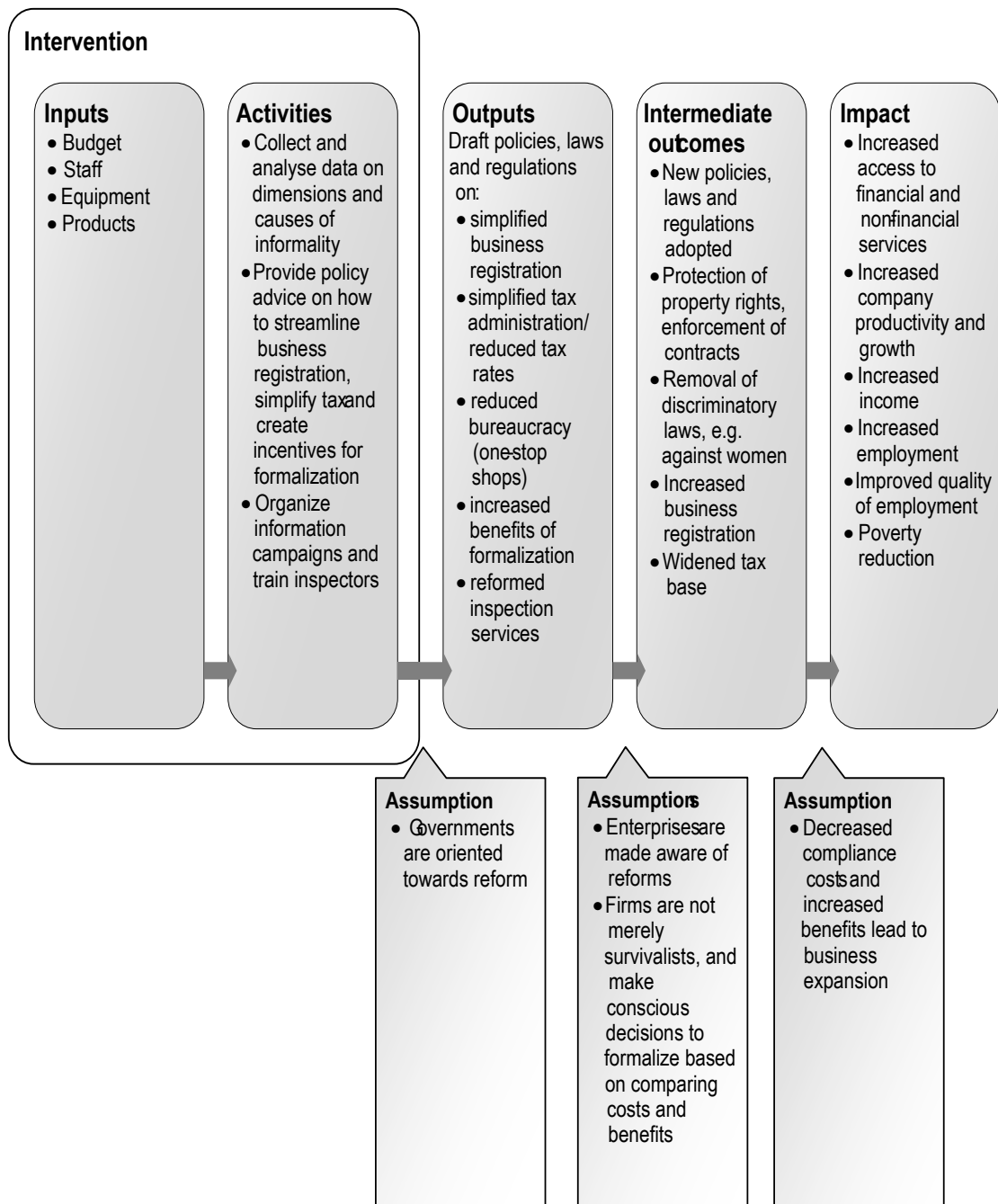
⁴⁰ Calculations by the ILO and COHEP.

⁴¹ For a typology of formalization policies by domain and the targeted costs and benefits of formalization, see K. van Elk and J. de Kok: *Enterprise formalization: Fact or fiction? A quest for case studies* (Geneva, Eschborn, 2014); or ILO Regional Office for Latin America and the Caribbean: *Policies for the formalization of micro and small enterprises in Brazil: Notes on policies for the formalization of micro and small enterprises* (Lima, 2014).

⁴² ILO: *Transitioning from the informal to the formal economy*, Report V(1), International Labour Conference, 103rd Session, Geneva, 2014.

innovation, increased formalization will create additional employment effects.⁴³ Finally, it is assumed that increased inspections combined with information campaigns can also contribute to higher formalization rates.

Figure 5.4. From projects to impact: Intervention model for enterprise formalization



Summarizing the global evidence

100. The empirical evidence on the relative effectiveness of different interventions for increasing the extent of formalization is still scarce. Only around ten empirically sound studies have been identified that assess whether such interventions have led to an

⁴³ See Grimm and Paffhausen, op. cit.

increase in enterprise formalization and have had an effect on enterprise performance and employment.⁴⁴ Most of these studies have an experimental or quasi-experimental design that takes into account what would have happened without the intervention. The studies mainly cover Latin America.

101. Overall, these studies show that the effects of formalization interventions are modest. Furthermore, the number of studies is still too small to enable any systematic conclusions to be drawn on whether specific types of formalization interventions work better than others. As documented by table 5 below, the main preliminary conclusions from the few empirical studies available can be summarized as follows:

- **Effect of business entry reforms on enterprise registration:** Business entry reforms (one-stop shops in Mexico) led to a 5 per cent increase in registration of new businesses. However, existing informal businesses did not become more likely to register.
- **Effect of business entry reforms on formalization of informal enterprises:** Two studies from Mexico and Peru show either small or short-lived effects.
- **Effect of information, waived costs and enforcement on formalization of informal enterprises:** Three studies show that information campaigns had no effect on the formalization rate. A mixed picture arises with regard to waived costs. One study shows a significant effect on formalization rates (10 per cent), while another shows no effect. One study also tested increased municipal inspections as a measure to increase formalization rates and found positive results (an increase in formalization of more than 20 per cent).

Table 5. Summary of studies on the causal effects of policies to promote enterprise formalization

Study	Policy or programme studied	Main results
Panel A: Effect of business entry reforms on number of enterprise registrations		
Bruhn (2011), Kaplan et al. (2011)	One-stop shop (combining municipal, state and federal business registration procedures) in urban areas in Mexico.	Reform increased business registrations by approximately 5 per cent and also increased employment; Bruhn shows that the increase in registered businesses was mainly due to previous wage earners opening new businesses.
Bruhn and McKenzie (2013)	One-stop shop in less populous municipalities in Minas Gerais, Brazil.	Programme led to a reduction in number of enterprises registering during the first two months of implementation, with no subsequent increase.
Cárdenas, Rozo (2009)	One-stop shop in six major cities in Mexico.	Reform increased business registrations by 5 per cent.
Panel B: Effect of business entry reforms on formalization of informal enterprises		
Bruhn (2013)	One-stop shop in urban areas in Mexico.	Some informal business owners become wage workers due to the reform, some register their business, but these effects are small.
Mullainathan, Schnabl (2010)	Municipal licensing reform in Lima, Peru.	Reform increased number of provisional licenses issued to informal enterprises, but many enterprises do not renew their license later.

⁴⁴ See Grimm and Paffhausen, op. cit.; K. van Elk and J. de Kok, op. cit.; and M. Bruhn and D. McKenzie: *Entry regulation and formalization of microenterprises in developing countries*, World Bank Group Policy Research Working Paper No. 6507 (Washington, DC, 2013).

Study	Policy or programme studied	Main results
Panel C: Effect of information, waived costs and enforcement on formalization of informal enterprises		
Alcázar et al. (2010)	Subsidy to informal enterprises in Lima, Peru, for the cost of obtaining a municipal licence.	Subsidized cost offer led to 10 to 12 per cent of informal enterprises obtaining a municipal licence.
Andrade et al. (2013)	Three interventions for informal enterprises in Belo Horizonte, Brazil: (a) delivery of brochures with information about registration process and potential benefits; (b) registration costs waived; (c) visits by municipal inspector.	Information and waived registration costs had no effect on formalization rate; municipal inspections increased formalization rate by 22 to 27 percentage points.
De Mel et al. (2013)	Provision of information and reimbursement of registration costs for informal enterprises in Sri Lanka.	Information and cost reimbursement had no effect on formalization rate.
Giorgi and Rahman (2013)	Delivery of brochures with information to informal enterprises in Bangladesh.	Information had no effect on formalization rate.

Source: Bruhn and McKenzie (2013), *op. cit.*

102. In addition to the abovementioned evidence, two case studies from Brazil are noteworthy because they involve large-scale national efforts to formalize informal enterprises. However, it should be noted that the studies do not compare enterprises that participated in formalization programmes with those that did not,⁴⁵ and it is therefore unclear whether the effects observed can be attributed to the interventions. The first case refers to the efforts of the Brazilian Government in 1996 to introduce a programme called SIMPLES, which simplified and reduced tax rates, social security contributions and tax regulations for micro and small enterprises. The programme had positive effects on the level of formality. The degree of formality among enterprises that were founded immediately after the launch of SIMPLES was higher than among enterprises that came into existence just before the launch. The number of operating licenses showed an increase of up to 12 per cent depending on estimation techniques, while the number of registrations with the tax authorities increased by 7 per cent. The effects tended to be greater for enterprises with paid employees than for enterprises without paid employees.⁴⁶ The effects were also greater for enterprises in their start-up phase than for already existing enterprises. Finally, formalized enterprises showed revenue and profit levels that were approximately 50 per cent higher than informal enterprises.

103. In 2008, Brazil introduced a further innovation offering individual micro-entrepreneurs a simplified registration procedure, together with a unified tax and social security scheme that allowed them to pay their contributions as a monthly lump sum. The programme addressed a total of 10 million informal self-employed workers. So far only descriptive statistical data are available, which show that 4 million individual micro-entrepreneurs were registered as of mid-2014.⁴⁷

⁴⁵ For a detailed description, see Van Elk and De Kok, *op. cit.*, or ILO Regional Office for Latin America and the Caribbean, *op. cit.*

⁴⁶ More than 85 per cent of Brazilian micro-enterprises do not have paid employees; see Van Elk and De Kok, *op. cit.*

⁴⁷ Based on figures received from the Brazilian SME support agency SEBRAE.

104. Given the limited state of knowledge on the effectiveness of formalization interventions, the key question of whether some interventions are more successful than others cannot yet be answered accurately. Still, some preliminary policy conclusions can be drawn:

- The available evidence is mainly confined to interventions directed at reducing the cost of formalization through business entry reforms, and it shows that this does not have the expected impact on enterprise formalization. There are fewer studies testing the effect of measures to decrease other significant costs of formalization or to increase the benefits related to it. Yet it is probably not so much the *costs of becoming formal* (time and money for registration) but the *costs and benefits of being formal* (taxes, social security contributions, access to social security) that is pivotal in an enterprise's decision to formalize. More studies are needed to test the effectiveness of measures to reduce the costs of being formal or to increase the benefits related to formalization. These new assessments need to go beyond documenting the effects on formalization and should cover other expected impacts such as improved enterprise performance and employment. Finally, only one experiment has tested the effectiveness of strengthening the enforcement of laws on enterprise formalization, and it showed good results. This measure should not be neglected and its effectiveness needs to be tested through studies that also take into account possible hidden costs such as “under the table” payments.
- It seems to be easier to formalize enterprises while they are being set up than to formalize enterprises that already exist. Therefore, it might be more effective to target efforts at start-ups.
- With regard to existing informal enterprises, more targeted measures should be tried. Growth-oriented informal enterprises and “constrained gazelles”⁴⁸ might benefit more from formalization than subsistence entrepreneurs, who might have neither the skills nor the motivation to become formal.
- Big pushes and packages combining several reform measures may work better than piecemeal approaches. Additional non-experimental econometric studies⁴⁹ on the magnitude of business entry reform that is required in order to achieve a significant impact on enterprise registration suggest that single reforms have to offer a large reduction of formalization costs in order to achieve a significant effect (at least a 50 per cent reduction in payments or 15 per cent reduction in the length of procedures). The synergies achieved when several reforms are combined mean that less drastic reductions in costs are required.
- Some of the oft-cited arguments in favour of enterprise formalization seem to be rather hypothetical. Existing studies find that formalization has no impact on the likelihood of obtaining a bank loan or government contracts. Information campaigns promising formalized enterprises access to finance or eligibility for public contracts need to be realistic. If they over-promise, they will undermine the efforts to increase formalization.

⁴⁸ See Chapter 2.

⁴⁹ L. Klapper and I. Love: *The impact of business environment reforms on new firm registration*, World Bank Group Policy Research Working Paper No. 5493 (Washington, DC, 2010).

Impact of ILO interventions

105. The ILO is running some technical cooperation projects to assist certain sectors in formalizing enterprises, such as the local transport sector in Kenya. So far, there have been no rigorous impact assessments of the effects of ILO interventions on the formalization of enterprises, except for two research studies on ILO projects that supported financial intermediaries in promoting enterprise formalization. The results are summarized below. As formalization has become one of the ILO's new strategic priorities, the Office should generate new evidence on what works to formalize enterprises.

106. With support from the ILO, the Indian microfinance institution ESAF introduced a combination of an awareness-raising campaign on enterprise formalization, non-financial business support services (between two and five days of training) and skills training (also two to five days) for clients that were considered to have the potential to grow. The objective was to see whether this intervention would have a positive impact on formalization and the social and economic situation of family enterprises. As a result of the intervention, formalization increased sharply (70 per cent among the target group, as compared to less than 10 per cent in the control group)⁵⁰ and business practices improved significantly (15 per cent increase in keeping accounts as compared to the control group). However, the research could not find a significant effect in terms of greater use of bank accounts, insurance services or government support schemes for family enterprises. Furthermore, the research found that the intervention had a significantly negative effect on monthly household income and employment. The reduction in household income can probably be explained by the introduction of more accurate bookkeeping practices, which helped the treatment group to arrive at more realistic estimates of income. With regard to the negative impact on employment, it is not clear whether formalization created an incentive to reduce employment or to under-declare the number of employees.

107. The ILO used a similar intervention to support the largest microfinance institution in Burkina Faso (RCBP), where it launched an awareness-raising campaign on formalization combined with a basic two-day training course on financial administration. As in the case of India, the objective was to increase formalization and enterprise performance. However, the effects on formalization were relatively moderate. The intervention had no impact on the formalization of enterprises, but there was a 10 per cent increase in the number of holders of an informal-economy registration card, a simplified way of registering an informal enterprise.⁵¹ There was some improvement in business procedures, documented by the keeping of separate accounts for business and private expenses. The intervention did not lead to improved access to financial services and did not have an effect on enterprise performance.

108. One important lesson learned as a result of these two interventions is that enterprise formalization interventions need to be integrated into government programmes that lead to a significant reduction in the cost of formalization and/or to an increase in the benefits

⁵⁰ For this and other results, see ILO: *Microfinance and Formalisation of Enterprises in the Informal Sector: Awareness raising campaign and BDS for the formalisation and strengthening of growth-oriented enterprises*, unpublished (2012).

⁵¹ For this and other results, see ILO: *La formalisation des entreprises de l'informel: Une étude d'impact sur la Formation et Sensibilisation à la formalisation des entreprises du secteur informel – RCPB au Burkina Faso*, [Formalization of informal enterprises: Impact study on training and raising awareness of formalization of enterprises in the informal sector – RCPB in Burkina Faso], unpublished (2012).

related to formalization. Running these interventions only through financial intermediaries might not have a sufficiently large impact.

5.5. Promoting improved working conditions and SME productivity

109. As has been highlighted by the ILO, a substantial number of poor people are in work. It is not the absence of economic activity that is the source of their poverty, but the less productive nature of that activity.⁵² Based on this analysis, the pursuit of productivity gains is essential in order to combat poverty and increase standards of living. When analysing the main drivers of productivity at the country level, it is clear that the most important single driver is enterprises becoming better at what they do.⁵³ Given the empirical evidence that SMEs are the main providers of employment but show significantly lower levels of productivity than large enterprises, they clearly have potential for raising living standards, but also limitations. For SMEs to increase wealth creation, they must improve the productivity of their existing activities or move into higher value-added activities.

110. It is in this context that the ILO has made SME productivity a new priority area of work, with a particular focus on the cause and effect relationship between working conditions and SME productivity. This focus arose from the observation that low levels of productivity often coexist with poor working conditions and that there is a need to better understand how they are linked.

111. Against this background, this section describes the intervention model, summarizes the global evidence on whether this particular and rather complex model of change works, and documents what is known about the impact of ILO interventions in this area. The section should not be interpreted in the sense that improvements in working conditions must always be justified by productivity increases. Working conditions are a priority of the ILO, independently of productivity, as is embodied in various international labour standards.⁵⁴ Instead, the aim here is to ascertain whether SME policies can create a win-win situation of improving both enterprise performance and working conditions.

Intervention logic

112. Pro-SME interventions aimed at improving the productivity of enterprises mostly focus on increasing total factor productivity.⁵⁵ This is achieved either through improvements in the quality of human resources (due to better education, vocational training, human resource management and/or working conditions) or changes in the efficiency of the production process (due to workplace innovations), or a combination of both. A third important factor influencing total factor productivity is improvements in the quality of physical capital (due to technological innovations). However, investments in new machinery are often very capital-intensive and this impedes the extent to which SMEs, which have limited access to finance, can rely on this route to higher productivity.

⁵² See various editions of *ILO World Employment Reports*.

⁵³ World Bank: *World Development Report 2013: Jobs* (Washington, DC, 2012).

⁵⁴ See the ILO's information system on international labour standards, NORMLEX.

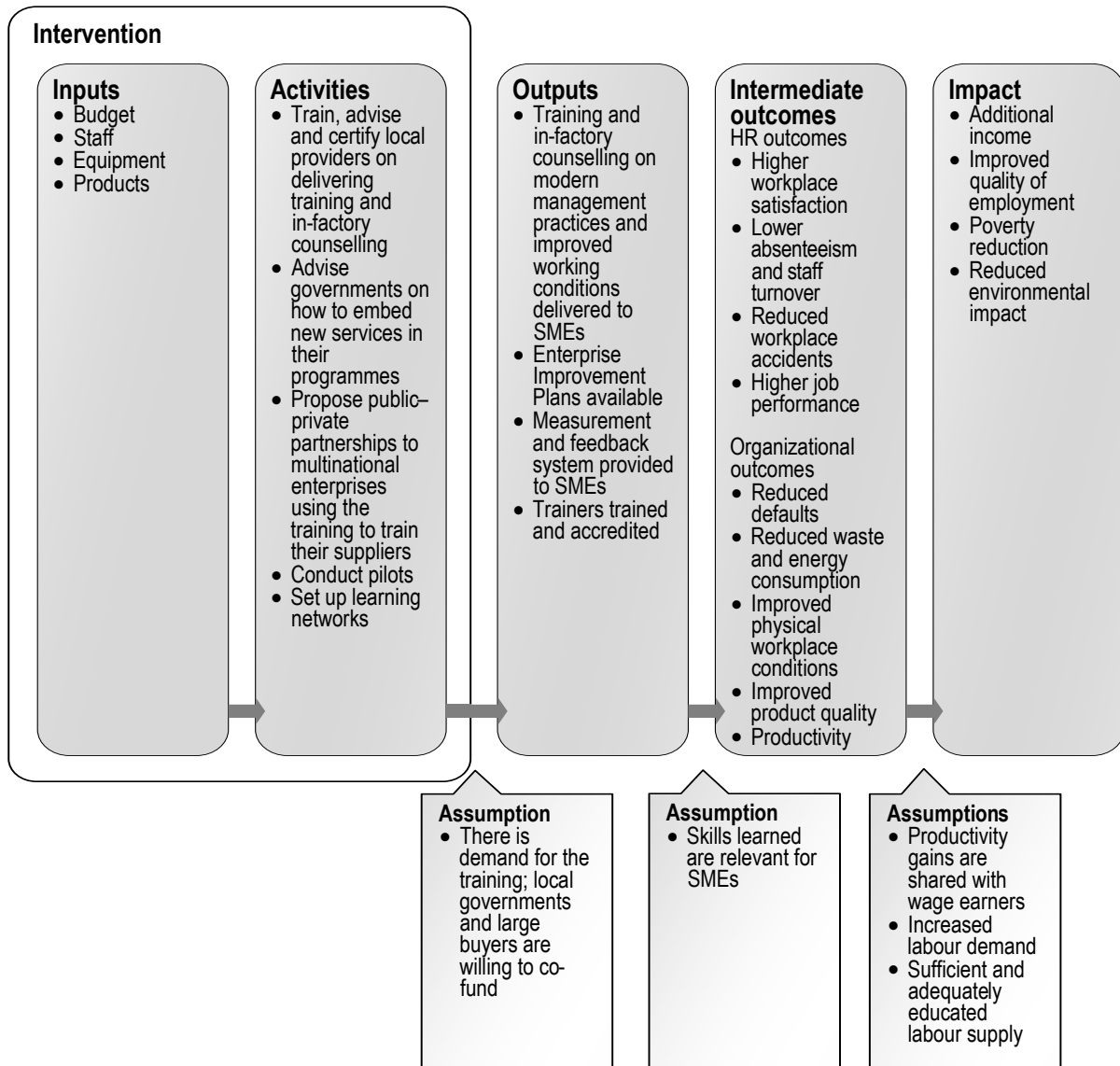
⁵⁵ Total factor productivity is the output per unit of combined labour and capital inputs. Changes in total factor productivity represent changes in the amount of output that enterprises can produce with a given quantity of capital and labour.

Therefore, the focus of interventions is typically on enhancing human resources and the production process, both of which are areas of intervention that are not overly costly and have the potential to provide quick returns.

113. With regard to how productivity increases can be achieved, there are two variations of the intervention model aiming at the same final impact:

- One approach says that **modern management practices** will lead to improved productivity. This will, in turn, lead to better enterprise performance and better working conditions as the final impact. This theory of change does not look at working conditions as a key intermediate outcome to increase productivity. It focuses on lean manufacturing, quality control, inventory management and human resources development.
- The other approach says that **improving working conditions** is also a means to the end of helping to increase enterprise productivity, thereby leading to the same final impact (improved enterprise performance and improved working conditions).

Figure 5.5. From projects to impact: Intervention model for promoting productivity and working conditions in SMEs



Summarizing the global evidence

114. This section attempts to summarize the available empirical evidence for both variants of the intervention model. With regard to the **effect of modern management practices on enterprise productivity**, there is considerable evidence that these interventions do lead to higher enterprise productivity and ultimately to improved enterprise performance and better working conditions. However, much of this research is related to developed countries only.⁵⁶ Nevertheless, there are also some interesting insights from emerging and developing countries which show that the introduction of modern management methods is related to improved working conditions. An econometric study based on factory audits of over 800 suppliers of a global sports goods manufacturer shows that closer cooperation of the multinational enterprise with suppliers on practices such as lean manufacturing and total quality management is more strongly related to improved working conditions than the monitoring of compliance with labour standards.⁵⁷ A key explanation given is that the introduction of these methods has positive spillover effects on working conditions. A recent experimental study testing these management practices in SMEs in an emerging country shows a strong impact on enterprise productivity and performance. The experiment of rolling out consulting services on modern management practices to medium-sized textile manufacturers in India shows that there was a 17 per cent increase in productivity in enterprises participating in the programme in the first year compared to non-participating enterprises in the control group.⁵⁸ The total increase in profits was US\$325,000 per plant per year, which meant that the cost of the intervention (US\$250,000) was already covered in the first year. After three years, many of the participating enterprises in the treatment group had opened additional production plants, indicating that additional employment was created. However, detailed data on the number and the quality of the jobs created were not collected.

115. With regard to the **effects of improved working conditions on SME productivity**, the empirical evidence is scarce. So far there have been no studies based on an experimental or quasi-experimental design. At the same time, there have been relatively few non-experimental econometric studies. Therefore, the ILO recently conducted a literature review on this topic,⁵⁹ which summarizes the findings of some 70 articles produced during the last decade. The study collected results on practices related to OSH, wages, training and working-time arrangements. Only studies that had undergone a credible refereeing process were included. In terms of research methodologies, the review accepted econometric studies and descriptive statistics, as well as qualitative research. Consequently, it is somewhat difficult to compare results. With this limitation in mind, the main findings of the review are summarized below.

116. On **OSH**, various studies confirm that a lack of awareness of the cost implications of occupational accidents and work-related ill health is common among SME owners. Research also points to a tendency for SME owners to be reactive rather than proactive.

⁵⁶ See, for example, N. Bloom and J. Van Reenen: "Measuring and explaining management practices across firms and countries", in *Quarterly Journal of Economics* (2007, 122(4)).

⁵⁷ R. Locke, F. Qin and A. Brause: "Does monitoring improve labor standards? Lessons from Nike", in *Industrial and Labor Relations Review* (2007, Vol. 61, No. 1).

⁵⁸ N. Bloom et al.: "Does management matter? Evidence from India", in *The Quarterly Journal of Economics* (2013, Vol. 128, Issue 1). The average enterprise size is 270 employees.

⁵⁹ R. Croucher et al.: *Can better working conditions improve the performance of SMEs? An international literature review* (ILO, Geneva, 2013).

Instead of adopting a preventive approach based on investments that pay off in the longer term, they often focus on short-term outcomes.

117. Nevertheless, there is growing evidence that confirms a link between good OSH practices and enterprise productivity, especially when these practices are an essential aspect of good business practice and quality management. However, evidence for a strong link across a sufficient range of cases is lacking, because of data limitations, difficulties in quantifying results, the long-term nature of this issue and the heterogeneity of SMEs.

118. When analysing the delivery of interventions in this area, a number of studies found that proactive measures are effective when they are sensitive to specific enterprise characteristics and sectoral differences. Good practices in this respect include the provision of advice through intermediaries such as sector associations, targeted industry programmes and the simplified implementation of OSH systems. Recent attempts to use supply chains in order to establish good OSH practices in SMEs is a promising approach. It has the advantage of specifically addressing barriers in SMEs, such as limited resources, lack of awareness and intense competition.

119. There is some evidence of a link between **training**⁶⁰ as a measure to increase managers' and employees' work-related skills and SME productivity. However, only a few studies have been able to provide persuasive evidence that training leads to increased enterprise productivity. It would appear that further mediating factors influencing SME productivity have to be taken into account. Such factors include the training methods (formal versus informal training), the staff groups targeted, the growth orientation of enterprises, the sectors and the training providers involved. The studies that are most persuasive in showing positive outcomes examined training as a part of improved human resource development practices and attempted to assess the long-term effects of training. However, this broader approach complicates the analysis and creates new methodological challenges for measuring results.

120. Research which focuses on the relationship between **wages** and productivity in SMEs is extremely scarce, and the few findings that are available are ambiguous. Whereas some research focusing on wages alone finds a positive association between wages and productivity, there is no evidence of a direct link. It seems that other factors have to be taken into account. In addition, reverse causality is very likely to exist. While wages may motivate employees (and hence have a causal effect on productivity), the ability of enterprises to pay wages is to a large extent determined by the productivity of the employees (and, hence, productivity has a causal effect on wages). In this respect, it is important to differentiate between wage levels and wage systems, where the wage system refers to the rules and factors that determine the wage level (such as whether it is related to experience and performance).

121. There is evidence for a positive association between the use of performance-related pay (as an important element of the wage system) and productivity. This evidence is provided by various studies that include performance-related pay as an integral element of so-called high-performance work systems. These systems are aimed at developing, retaining and motivating the workforce. Typical elements of such systems include teamwork, quality circles, training and career development, appraisals and performance-

⁶⁰ It should be noted that, in this context, training does not include education or initial vocational training.

related pay.⁶¹ High-performance work systems are more prevalent in developed countries.

122. Studies on **working time** which focus on SMEs are scant. Research on long hours and overtime has found that these practices, if exercised over a prolonged period of time, have negative short-term effects, such as increased risk of injury, and long-term adverse health effects. Both lead to decreased productivity. Other research indicates that moderate overtime can have positive effects on productivity if it is voluntary and is appropriately remunerated.

123. The relationship between **freedom of association or collective bargaining** and productivity has been an area of study for several years; however, there is no empirical research specific to SMEs.

124. Overall, the evidence on the relationship between improvements in working conditions and increases in SME productivity is positive for OSH and inconclusive for other areas. It is not clear whether individual or stand-alone interventions on improving working conditions and productivity can deliver the expected results. The empirical support for the intervention model is much stronger when **bundles of human resource management practices** are assessed. These studies relate certain combinations or packages of the abovementioned interventions to different indicators of enterprise performance. There is considerable evidence that packages of interventions are positively associated with measurements of enterprise performance such as productivity or profits. Recent ILO research in Viet Nam points in the same direction. Based on Vietnamese enterprise-level data covering all registered non-state manufacturing companies, the study finds a clear positive link between social security provision (measured by the share of workers with access to the fairly comprehensive package of mandatory social and health insurance) and enterprise performance of SMEs (measured in terms of revenues or profits).⁶² The main explanation given is that such a comprehensive package enhances the motivation of the workforce, thus eliciting higher levels of effort.

125. The main explanation provided for the higher effectiveness of package approaches as compared to stand-alone interventions is that specific combinations of practices (for example, training on quality control combined with performance-related pay) yield synergies. The effect of the bundles of measures is larger than the sum of individual interventions. In other words, it is not the application of individual practices that matters, but rather the application of a group of connected practices.

126. **A key conclusion from the overview of the global evidence** is that, independently of the intervention model, a greater integration of initiatives to improve working conditions and to upgrade core management practices is needed. This systemic approach of elevating and integrating working conditions into a business's core operations can be expected to produce better results for enterprise productivity. The approach of bundling interventions to improve working conditions is ultimately not very different from the approach focusing on modern management practices, and the two should be combined. This means that future pro-SME interventions and research on their effectiveness should concentrate less on establishing the effect of individual practices (wages, training and working times) on the productivity of enterprises and should instead

⁶¹ M. White et al.: "High-performance' management practices, working hours and work-life balance", in *British Journal of Industrial Relations* (2003, Vol. 41, No. 2).

⁶² N. Torm and S. Lee: *Does better protection improve enterprise performance? Social security and firm performance in the case of Vietnamese SMEs*, unpublished (2013).

focus on testing the effectiveness of integrated packages of connected practices and their effect on productivity and working conditions as a final impact.

127. The limitation of the findings is that they are mainly based on studies involving large enterprises from developed countries. Further research is required in order to determine whether the same also applies to SMEs and in the context of developing countries. A related question is whether SMEs in developing countries require different combinations of interventions and practices aimed at improving working conditions. Given the predominance of mostly informal management practices in small enterprises, it is assumed that integrated interventions which require a strategic view of human resource development can best be applied in medium-sized enterprises.

Impact of ILO interventions

128. The ILO has been running several programmes aimed at improving working conditions and productivity in micro-enterprises as well as in SMEs. With support from the ILO, the Indian microfinance institution BASIX rolled out a 16-hour training course for small farmers, providing basic orientation on OSH and productivity.⁶³ The roll-out was accompanied by a quasi-experimental impact assessment. The results of this research show a significant decrease in self-reported workplace injuries (30 per cent lower in the treatment group), a weak improvement in working conditions (as measured by daily work-hours, regular breaks or fixed rest days), a strong effect on stabilizing net monthly income (beneficiaries managed to keep their incomes stable, while the control group experienced a reduction in income of 70 per cent)⁶⁴ and no effects on household wealth.

129. For SMEs, the ILO has been running two major programmes for the last five years. First, Sustaining Competitive and Responsible Enterprises (SCORE) is a modular training and in-factory counselling programme on workplace cooperation, quality management, cleaner production, human resource management and OSH.⁶⁵ SCORE is based on an integrated approach combining modern management practices and improved working conditions. It is aimed at medium-sized, lower-tier suppliers in national and international supply chains with a strong focus on manufacturing. Second, the ILO's training and advisory programme for improving social dialogue, working conditions and productivity (SIMAPRO) started out as a programme for the sugar industry in Mexico – a sector characterized by poor working conditions and frequent labour conflicts. The programme has since been expanded to five additional Latin American countries and further sectors, such as tourism.

130. The ILO has not yet conducted rigorous impact assessments on the effects of interventions such as SCORE and SIMAPRO, but some initial steps have been taken. SCORE has produced a results chain based on the DCED's Results Measurement Standard.⁶⁶ This work will undergo an external audit. Furthermore, an experimental

⁶³ Based on the ILO training package for improving working and living conditions of agricultural families, Work Improvement in Neighbourhood Development (WIND).

⁶⁴ In 2010, a severe drought in the state of Andhra Pradesh and over-indebtedness of farmers led to social unrest and the Andhra Pradesh microfinance crisis; see A. Jaeggli and H. Yousra: *Microfinance and working conditions: Increasing workplace safety through safety education*, ILO Social Finance Programme, unpublished (2014). The results are of limited credibility, as the quasi-experiment was rolled out in two branches of a microfinance institution, with clients of a third branch serving as control group; the methodology cannot fully rule out differences between treatment and control group.

⁶⁵ For details about this programme, which currently covers seven emerging countries, see: www.ilo.org/score.

⁶⁶ For details of the DCED Results Measurement Standard, see section 5.7 below.

impact assessment to be rolled out in 2015 has been designed for one country. Results from SCORE's monitoring system show that the intervention works at the level of intermediate outcomes. Half of the 400 enterprises participating in the programme have so far reported cost savings (of up to US\$15,000 in the first two months), while 80 per cent of enterprises report reductions in defects (of an average of 10 per cent). Absenteeism has decreased on average by 4 per cent. Along similar lines, SIMAPRO reports a 50 per cent reduction in the severity rate of accidents in sugar mills, a 32 per cent reduction in food waste in restaurants, a 4 percentage-point increase in workplace satisfaction, and a 3 per cent increase in employment in 100 SMEs.

131. Since the ILO has decided to make working conditions and productivity in SMEs a priority area of work, additional evidence on the effectiveness of this approach is being generated. This is necessary in order to provide solid and fact-based policy advice.

5.6. Value chain development

Intervention logic

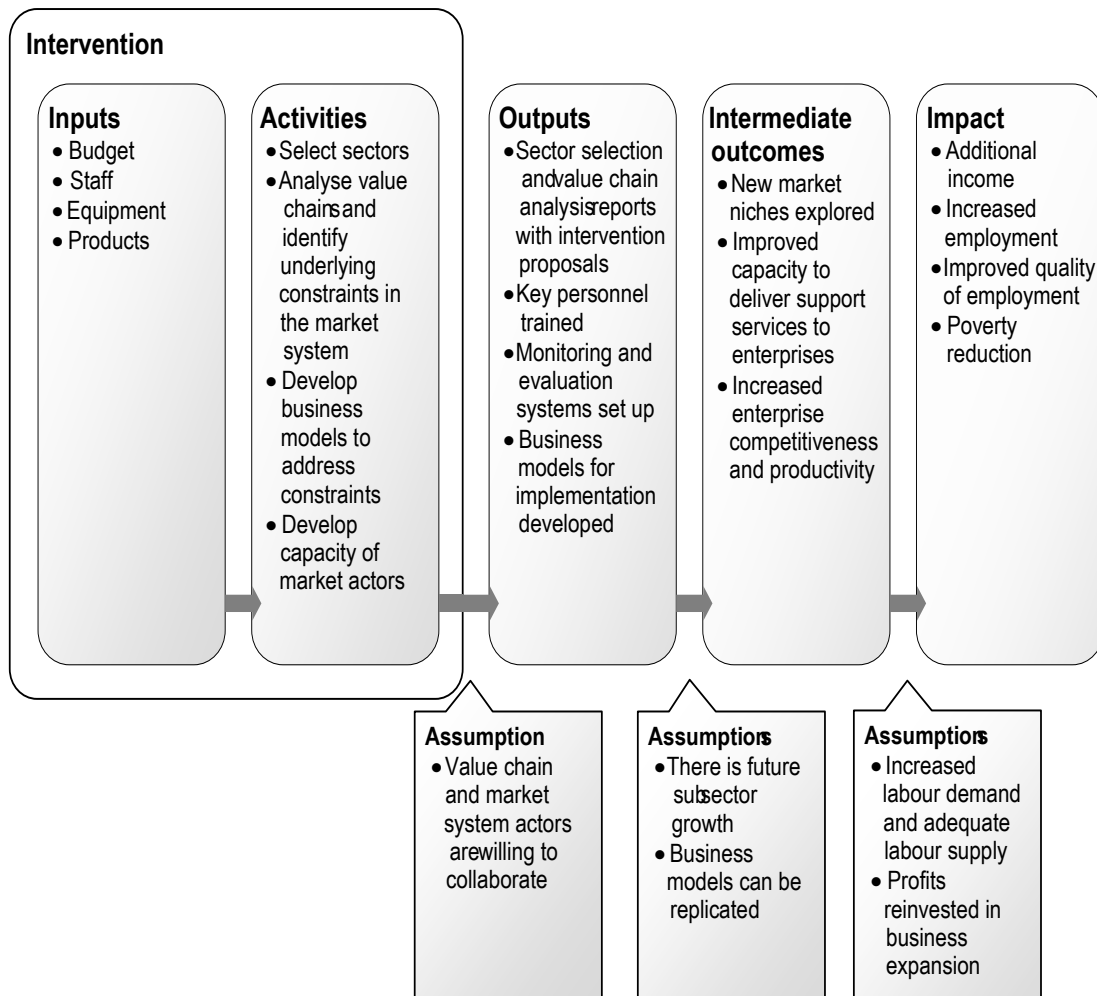
132. This section focuses on what is known about the effects of value chain development interventions on employment creation and job quality for SMEs.⁶⁷ Value chain development approaches are becoming increasingly popular as they are expected to make substantial contributions to income generation and job creation because of their strong emphasis on scale and financial sustainability.⁶⁸ The basic philosophy of these interventions has been to aim for large-scale impact by improving the functioning of entire markets or sectors rather than only targeting individual market actors. However, this makes such interventions rather complex and creates greater challenges for results measurement.

133. Many value chain interventions focus on strengthening backward linkages to domestic industries once foreign direct investment has been attracted. Another important area of action has been to link SMEs to multinational enterprises and global supply chains by attracting foreign direct investment, revising trade policies and promoting supplier development. This report does not cover multinational enterprises and global supply chains, which will be a subject of discussion at the 105th Session of the International Labour Conference in 2016.

⁶⁷ A value chain describes the full range of activities that are required to bring a product or service from conception through the intermediary phases of production and delivery to final consumers. Value chain development attempts to alter the structures, systems and relationships in the chain.

⁶⁸ See, for example, the success stories on the DCED website: <http://www.enterprise-development.org/page/stories#VCD>; or J. Mitchell, J. Keane and C. Coles: *Trading up: How a value chain approach can benefit the rural poor* (London, 2009).

Figure 5.6. From projects to impact: Intervention model for value chain development



Summarizing the global evidence

134. Value chain development is becoming a widely used tool in poverty reduction and private sector development. However, there is still a need for rigorous measurements of the results of these interventions. In contrast to highly standardized pro-SME interventions such as training, value chain interventions pose particular challenges for impact analysis. These difficulties include the following:

- Value chain interventions often affect a whole subsector in a country or region, which makes the construction of a counterfactual scenario very challenging and in some cases impossible. Results measurement methodologies to overcome this problem are being established by several development agencies.⁶⁹
- Likewise, the indirect nature of value chain development interventions (facilitation instead of direct intervention) makes it more difficult to measure impact. It is also more difficult to attribute observed outcomes to a specific intervention than in the case of providing training and credit to target beneficiaries.

⁶⁹ See DCED: *DCED Standard for Results Measurement*, <http://www.enterprise-development.org/page/measuring-and-reporting-results>.

- Value chain development projects typically address several underlying constraints of market systems at the same time. One intervention could be working on improving skills while another in the same value chain could be working on microfinance or improving business registration. This heterogeneity of value chain interventions makes direct comparisons and experimental impact assessments difficult.

135. Therefore, it is not surprising that a recent study by the UK Department for International Development looking at existing evaluation methods for market development projects concluded that evaluations of projects working with value chains were weak in their consideration of sustainable changes in market systems.⁷⁰

Impact of ILO interventions

136. The ILO's work on value chain development has largely been on rural value chains and supply chains in agricultural markets and services such as tourism. The Organization is currently implementing 20 projects with an overall budget of US\$50 million. In terms of the **effectiveness of ILO interventions in this domain**, rigorous evidence on the income or job creation effects of its value chain interventions is not yet available.⁷¹ There are, however, some surveys from projects that indicate tangible results. One good example is the ILO's Enter-Growth project in Sri Lanka, which aimed to develop the horticulture and dairy sector in four districts of the country between 2005 and 2009. The project reached out to 52,000 businesses and resulted in a tripling of household incomes.⁷² However, these figures are based on projections and are not very robust. Therefore, the ILO recently launched a knowledge generation project to measure the labour market effects of value chain interventions. The project, which will run until 2017, aims at producing robust results and finding satisfactory solutions to bridge the attribution gap. It is currently working with ILO projects in Peru, Timor-Leste and Zambia as well as with non-ILO projects to help them to improve their monitoring and results measurement systems.

5.7. New trends in SME policies

137. SME policies have been a major part of the economic policies of developed and developing countries alike for several decades now. They are perceived to be important in terms of creating employment, fostering competition and innovation, and contributing to economic growth. Different approaches have evolved and have been tested, ranging from macro-level interventions through to support to individual enterprises, as well as improvements to the enabling environment and more systemic approaches of developing entire markets.⁷³

138. Since there is a broad consensus on the important role of SMEs, and of the private sector in general, current innovations are based less on new paradigms or new technical

⁷⁰ Itad: *Review of M4P evaluation methods and approaches*, 2013.

⁷¹ Training and advisory services on how to integrate SMEs into local and global value chains are one of the most recent ILO products promoting SMEs. The product is facing a strong and increasing demand; see: www.ilo.org/valuechains. The ILO also offers training material targeted at certain sectors, such as the toolkit on reducing poverty through tourism.

⁷² S. Barlow: *The Enter-Growth project – Sri Lanka: Applying a market development lens to an ILO local enterprise development project*, ILO Employment Report No. 11 (2011).

⁷³ For an overview of changing approaches see, for example, G. Buckley, J.M. Salazar-Xirinachs and M. Henriques: *The promotion of sustainable enterprises* (Geneva, ILO, 2009).

areas of intervention, but instead involve new modes of delivery that reflect the quest for greater outreach and effectiveness. In other words, the current discussion on innovative ways to promote SMEs is less about doing the right things than about doing things right. The only exception is the new technical area of greening SMEs, which is addressed at the end of this section.

Rigorous results measurement

139. The practice of more rigorous monitoring and results measurement – which considers attribution up to the level of impact on enterprise incomes and jobs – is one of the key recent trends in the delivery of SME policies. As with most other development interventions, SME policies and related programmes are under increasing pressure to provide credible measurement of, and transparent reports on, the results achieved. Not only are governments and donor agencies keen for their taxpayers to see concrete results from their investments, but practitioners are also interested in finding out more about whether and why their interventions are (or are not) having an impact.

140. Inspired by the work of the Poverty Action Lab,⁷⁴ one important movement towards more rigorous results has been to conduct experimental or quasi-experimental evaluation designs which help to estimate statistical counterfactuals. In other words, the aim is to reconstruct what would have happened without the intervention, usually through using a control group. The SME initiative at Innovations for Poverty Action alone lists 40 ongoing projects that assess the effects of different pro-SME interventions.⁷⁵ The International Initiative for Impact Evaluation (3ie), another leading non-profit organization promoting the use of rigorous impact evaluations, is working on a new systematic review of the impact of business support for SMEs on enterprise performance in low- and middle-income countries.⁷⁶ As reported above, the ILO has five ongoing experiments to evaluate different SME support programmes.

141. Another new and relevant initiative in promoting more credible internal results measurement has been introduced by the DCED through its Results Measurement Standard.⁷⁷ The standard, which was first developed in 2008, is a framework which helps practitioners to:

- clearly articulate their intervention hypothesis, using results chains to complement logical frameworks; and
- systematically set and monitor indicators which show whether changes are occurring and, as far as possible, to establish whether there is a causal connection between them.

142. The DCED secretariat also coordinates an audit service, where programmes can choose to have their monitoring system assessed externally and objectively. This is intended to enhance the credibility of reported results, and to obtain recognition from donors and development agencies that a project is engaged in high-quality results measurement.

143. Demand for the DCED standard is growing. Over 100 private sector development projects and programmes are currently using the framework. This has largely been

⁷⁴ See: <http://www.povertyactionlab.org>.

⁷⁵ See: <http://www.poverty-action.org/sme>.

⁷⁶ L. González et al.: *The impacts of business support services for small and medium enterprises on firm performance in low- and middle-income countries: A systematic review* (3ie, 2014).

⁷⁷ DCED: *DCED Standard for Results Measurement*, op. cit.

driven by donors such as the UK Department for International Development, the Australian Department of Foreign Affairs and Trade, the Danish Ministry of Foreign Affairs and the Swedish International Development Cooperation Agency. The ILO has been at the forefront of multilateral agencies that have moved towards monitoring and results measurement in line with the DCED standard. Currently half a dozen projects as diverse as those supporting tourism in Myanmar, improving working conditions and productivity in SMEs (SCORE), promoting youth and women's employment in Morocco and Zambia, and supporting rural value chain developments in Timor-Leste are adopting the standard.

144. Results measurement in line with the DCED standard does not usually provide the same level of statistical rigour in addressing attribution as experimental impact assessments. However, with its emphasis on balancing the practical considerations of the available time, resources and expertise with an acceptable level of rigour, and its focus on plausible – rather than scientific – attribution, the standard is arguably more relevant and applicable to a much wider range of SME interventions. The standard can also be combined with experimental impact assessment.

145. Although results measurement for SME interventions is still at an early stage, within a few years this and other initiatives will have increased the evidence on what works. In addition, the ILO recently launched a knowledge generation project to measure the labour market effects of value chain interventions.

Partnerships with business

146. Another new trend in development cooperation is the emergence of partnerships between donors and businesses that aim to leverage enterprises' resources in order to achieve development results. These partnerships are considered to be an increasingly important tool for promoting private sector development. Leveraging private sector activity and finance for development is also supported by recent international forums such as the Fourth High Level Forum on Aid Effectiveness, several G20 forums and the European Commission's Agenda for Change.⁷⁸ The basic rationale is to share the costs and risks of enterprises' investments in developing countries by pursuing the dual goals of promoting the enterprises' core business and of creating an additional development impact that would not have been realized without the donor support.⁷⁹

147. This approach is particularly relevant for SME promotion, since it very often includes the promotion of forward and backward linkages between SMEs in developing countries and large corporations from abroad. The successful examples very often refer to partnerships in the agricultural sector that reach out to thousands of small and poor contract farmers.

148. From the donors' perspective, these partnerships seem to be a good way to increase outreach, to achieve sustainability through businesses that continue their work after the completion of the donor support, and to couple development cooperation objectives with economic benefits for the business community at home. The enterprises' main motivation is to make use of the donors' expertise, infrastructure and funds in order to help explore new markets or to improve the social and environmental sustainability of

⁷⁸ B. Byiers and A. Rosengren: *Common or conflicting interests? Reflections on the private sector (for) development agenda*, European Centre for Development Policy Management, Discussion Paper No. 131, 2012.

⁷⁹ M. Heinrich: *Donor partnerships with business for private sector development: What can we learn from experience?* (DCED, 2013).

their business.⁸⁰ Mechanisms being used range from matching grants for companies through to broader multi-stakeholder coalitions for developing entire sectors or clusters.

149. One of the key challenges faced by donors is the need to demonstrate additionality: that is, they have to be able to show that the results achieved through a partnership programme are significantly greater than the results the enterprise would have achieved without the programme. All in all, credible information on additionality is sparse and there is a need to harmonize approaches and ensure rigour in implementing this concept.⁸¹ The same holds true for measuring the results of such partnerships. Overcoming these two challenges will be crucial in convincing the critics who see conflicts of interest between development and commercial interests, and in showing that this new approach works.

150. The ILO has also reviewed its approach to cooperation with business and has adopted a new strategy for wider ILO engagement with the private sector.⁸² The strategy focuses on supply chain policies and practices, international initiatives on enterprise behaviour, and joint knowledge generation by the ILO and enterprises. The ILO's main motivation is not to raise funds from enterprises, but to benefit from their know-how and to increase the outreach and the sustainability of activities that are related to the ILO's objectives and are also relevant for enterprises. This approach is still too new to be evaluated properly. However, it could be highly relevant for ILO programmes aimed at including local SMEs from developing countries in local or global supply chains.

Environmental sustainability and greening SMEs

151. Environmental sustainability, in particular arresting climate change, is rapidly gaining ground as a global concern. It is also increasingly being recognized as an opportunity for more sustainable and inclusive economic growth.⁸³ Since SMEs account for the majority of enterprises and employment in the world, their transition to sustainable business practices will be crucial to achieving sustainable development in developed and developing countries alike.

152. On the one hand, SMEs need to be able to cope with the challenges of increasing resource scarcity, higher costs and more stringent environmental standards. On the other hand, they need to be able to seize the opportunity of rapidly growing markets for environmental goods and services. This includes markets for green technology and energy efficiency, which are among the fastest growing in the global economy. According to one study, even during the Great Recession of 2007–10, this segment grew at 11.7 per cent per year to reach a total volume of €2,000 billion in 2011. It is expected to rise further to €4,400 billion by 2025, an increase of 5.6 per cent per year.⁸⁴

153. SMEs will be a major source of that demand. A recent study estimates that the demand for clean tech products and services of SMEs in developing countries alone will

⁸⁰ *ibid.*

⁸¹ *ibid.*

⁸² ILO: *Strategy for wider ILO engagement with the private sector*, Governing Body, 321st Session, June 2014, GB.321/INS/6.

⁸³ See ILO: *Working towards sustainable development: Opportunities for decent work and social inclusion in a green economy* (Geneva, ILO, 2012); or OECD Working Party on SMEs and Entrepreneurship: *SMEs and Green Growth: Promoting sustainable manufacturing and eco-innovation in small firms*, Issues Paper 3 (Paris, 2010).

⁸⁴ German Federal Ministry for the Environment, Nature Conservation and Nuclear Safety: *Green tech made in Germany 3.0: Environmental technology atlas for Germany* (Berlin, 2012).

be US\$1.6 trillion in the next ten years.⁸⁵ With their flexibility and innovation, SMEs can also play a prominent part in these markets. In Germany, for example, 90 per cent of the producers of environmental technology are SMEs.⁸⁶

154. For the most part, however, SMEs seem to be less well prepared for the transition to a green economy than larger companies. An EU survey shows that larger companies are considerably more likely to save energy than SMEs (82 per cent compared to 64 per cent). While half of all large corporations in the EU have an environmental management system in place, only a quarter of SMEs have taken such specific action. With regard to product innovation, the situation is very similar. Only a quarter of SMEs offer green products or services, while more than 40 per cent of large companies are already present in green markets. Although there are no comparable data for SMEs in developing countries, it can be expected that these businesses are even less likely to engage in the transition to a green economy.

155. As consumers and the private sector pay more and more attention to the greening of products, services and supply chains, governments, donors and multilateral agencies are increasingly integrating environmental sustainability into SME promotion. In doing so, they are employing a variety of approaches, models and instruments. Broadly, two approaches are emerging: governments and donors are either mainstreaming environmental considerations into any initiative to promote SMEs or they are specifically targeting SMEs to green their business operations and to explore markets for green products. This brief section focuses on the latter approach.

156. The shared objective of these efforts is to foster economic advancement and development while improving efficiency in the use of natural resources and preventing further damage to the environment.⁸⁷ It is also widely agreed that in order to achieve this objective, the approach has to catalyse investment and innovation, leading to new economic opportunities.

157. A recent stocktaking analysis of 120 interventions from more than a dozen bilateral and multilateral agencies provides an initial overview of the most common approaches to greening and indicates some emerging lessons.⁸⁸ The report documents the rapid expansion of greening in private sector development, but recognizes that it is still too early to assess any long-term results.

158. It should be noted that approaches for greening SMEs do not differ substantially between developing, emerging and developed economies, which illustrates the global relevance of and worldwide interest in the topic.⁸⁹

⁸⁵ World Bank, InfoDev: *Building competitive green industries: The climate and clean technology opportunity for developing countries* (Washington, DC, 2014).

⁸⁶ German Federal Ministry for the Environment, Nature Conservation and Nuclear Safety (2012), op. cit.

⁸⁷ DCED: *Green growth and private sector development: Stocktaking of DCED experiences*, Final report for the Green Growth Working Group of the Donor Committee on Enterprise Development (2014).

⁸⁸ *ibid.*

⁸⁹ See, for example, European Commission: *Green action plan for SMEs* (Brussels, 2014), which lists very similar types of intervention as the abovementioned DCED study.

159. A tentative typology of interventions is proposed below:

I. An enabling business environment

- **Policies promoting environmental sustainability, a green economy and green growth:** Most programmes have a component supporting governments in developing a regulatory framework. This requires a mix of policies to set prices at the correct level (eco-taxes, smart use of subsidies, or tradable permits) or to introduce direct regulations in the case of market failures.⁹⁰ This approach has potentially the biggest impact; however, there is as yet no evidence on its effectiveness.
- **Green credit lines and investment funds:** Several development banks are running credit lines or investment funds for SMEs that wish to invest in energy efficiency or renewable energy projects. Initial experiences show that, as is the case for other credit lines, access to green funding needs to be complemented by training and advisory services for enterprises as well as for financial intermediaries.

II. Green business practices

- **Promoting green operations in SMEs:** This approach promotes cleaner production and greater resource efficiency in SMEs. It usually attempts to make a business case for greener operations by demonstrating the financial benefits of certain investments or behaviours.⁹¹ This is typically done through training and in-factory counselling. Emerging lessons clearly show that cost savings need to be convincingly communicated and demonstrated in order to create sufficient demand for this service. The limited investment capacity of SMEs can be an impediment if large and long-term investments are needed. Additional scale can be achieved if SMEs are matched with large international buyers and can clearly see that greener management practices lead to larger and longer-lasting contracts with buyers. One specific case is training and advisory services on green standards and certification schemes. It is worth noting that the proliferation of these standards represents a particular challenge.

III. Innovation and market development

- **Green market and value chain development approaches:** Market development interventions are not a new instrument in SME promotion. The basic philosophy of these interventions has been to achieve large-scale impact by improving the functioning of entire markets or sectors rather than only targeting individual market actors. The innovation in this approach is the attempt to use value chain interventions to introduce and promote the adoption of new green products or production processes.⁹² So far, there has been very little experience with green value chain approaches and it is too early for initial lessons to be drawn.

⁹⁰ A good example is the Partnership for Action on Green Economy (PAGE), a seven-year programme launched in 2013 to assist a total of 30 countries in their efforts to make the transition to environmentally viable and socially inclusive economies. It uses the joint expertise of the ILO and the United Nations Environment Programme (UNEP), the United Nations Development Programme (UNDP), the United Nations Industrial Development Organization (UNIDO) and the United Nations Institute for Training and Research (UNITAR).

⁹¹ Some good examples are the ILO's cleaner production module under its global programme to improve productivity and working conditions in SMEs, and the training on adopting resource-efficient business practices for SMEs in India offered by GIZ.

⁹² Some good examples are the Africa Biogas Partnership Programme supported by the Netherlands, and the One UN project on promoting green jobs in the building construction sector, led by the ILO and supported by Finland.

- **Promotion of green technology start-ups:** This approach aims at promoting new green products and business models, usually through brokering partnerships between foreign producers of innovative green products and local partners. Local start-ups could also be encouraged to adopt green products and business models through incubators or business plan competitions.⁹³

160. Given the increasing attention to climate change and the growing concern about environmental hazards and resource scarcities, greening will most likely remain a rising trend in SME promotion among governments and donors. In addition, SME organizations increasingly request government support, realizing the potential cost savings and competitive advantages that can be gained from moving to a greener economy. In view of the considerable resources being invested, it is crucial to rapidly develop clear theories of change, solid indicators and rigorous impact assessments before further scaling up the different approaches to promoting green growth for SMEs.

Focusing on high-growth enterprises

161. As documented in this report, start-ups and young enterprises create the majority of new jobs. However, most entrepreneurship development interventions in developing countries focus on very small enterprises and self-employed people, reflecting the desire to target high-need, marginalized populations. These interventions can have measurable effects on employment, as documented in this chapter, but the effects are probably lower than for the young high-growth enterprises.

162. Consequently, a small but increasing number of initiatives⁹⁴ are now developing support programmes that are aimed at these high-potential enterprises and that rely more on individual entrepreneurship characteristics.⁹⁵ The proponents of these initiatives argue that most entrepreneurship development programmes do not cater adequately to high-potential enterprises, and instead focus on providing basic training or microfinance at the planning phase of setting up a business. This basically consists of generating a business idea and imparting some basic managerial skills to develop a product or business model. According to the critics of these general programmes, they often overlook the validation and preparation phases, which are particularly risky for high-potential start-ups. These new enterprises have not yet established a foothold in the market and need to invest significant time and resources in validating their business concept. It is further argued that validation and preparation are the under-served phases of the business cycle and that they require refined and sophisticated financial and non-financial support services that go beyond the mere provision of basic management skills and microfinance.

163. The enhanced support required at the validation and preparation phases includes non-financial services such as specialized technical assistance (accounting, legal

⁹³ The ILO has developed and tested ways to promote green start-ups at the request of the Governments of China and Kenya.

⁹⁴ The Aspen Network of Development Entrepreneurs (ANDE), a quickly growing network of development practitioners, was established in 2009 to promote small and growing businesses (SGBs), defined as enterprises with five to 250 employees and ambition for growth. Typically, SGBs seek growth capital from \$20,000 to \$2 million.

⁹⁵ This request for filtering based on individual entrepreneurial characteristics is in line with recent findings that entrepreneurship characteristics (human capital, motivation, risk-taking ability and international exposure) are more important for the success of upgrading an SME than enterprise characteristics (size, sector, formality), personal or professional networks, and the business environment; see A. Hampel-Milagrosa, M. Loewe and C. Reeg: "The entrepreneur makes a difference: Evidence on MSE upgrading factors from Egypt, India, and the Philippines", in *World Development* (2015, Vol. 66).

services, business advice), physical incubation (office space, facilities, product testing), mentorship and market research. New financial services or co-investments through angel investors' networks are also required.⁹⁶ The entire system of enterprises, institutions and networks that identifies, trains, connects, funds, enables and creates public awareness of entrepreneurs is referred to as the entrepreneurship ecosystem.⁹⁷ The concept behind this new term is no different from market development approaches aiming to improve the functioning of entire markets or sectors rather than only targeting individual market actors.

164. The merit of the new approach is certainly that it draws the attention of development practitioners to the small but highly relevant segment of high-growth start-ups, which can be expected to make considerable contributions to employment creation. It might be interesting to include them in existing initiatives supporting micro-enterprises and self-employed people. While there is solid macro-level evidence of the substantial effects these enterprises have on job creation, there is so far no evidence that enterprise-level interventions work and that the expected benefits are higher than the cost of sophisticated support services. Two critical questions have not yet been answered. The first is how these high-potential start-ups should be selected. Most of the new initiatives focus on start-ups in strategically prioritized sectors such as information and communication technologies and neglect high-potential enterprises in other sectors. The second unanswered question is how to offer services such as mentorship on a larger scale. Currently, the ILO does not have specific programmes for high-growth start-ups.

⁹⁶ Springfield Centre: *Start Up! – A proposed new DFID programme*, unpublished, 2014.

⁹⁷ See S. Koltai, V.K. Mallet and M. Musprat: *Ghana entrepreneurship ecosystem analysis*, final report, prepared for the UK Department for International Development, unpublished, 2013; or D. Isenberg: "The big idea: How to start an entrepreneurial revolution", in *Harvard Business Review* (June 2010).

Chapter 6

Suggested points for discussion

The aim of the discussion on SMEs and decent and productive employment creation is for the ILO to generate a better understanding of, and respond more effectively to, the diverse realities and needs of its Members, using all means of action at its disposal. The results of the discussion should lead the ILO to confirm or adjust its priorities accordingly.

1. What is the contribution of SMEs, and specific differentiated segments within SMEs, to employment creation and what is the quality of employment in SMEs?
2. What are the main constraints faced by different segments of SMEs and their workers and what has to be done to increase their contribution to decent and productive employment creation?
3. What SME policies and related measures produce good results in terms of creating additional and decent employment through sustainable enterprise development? How have these policies dealt with the large heterogeneity of SMEs?
4. What are the roles of governments and of the social partners in promoting policies for decent and productive employment in different SME segments?
5. Which SME policies and related measures of the ILO have worked and which have not? What gaps are there in ILO knowledge, products, capacity building and strategic partnerships? What should be continued and scaled up, and what should be added?

Appendix

Overview of findings for interventions using ILO products for entrepreneurship training and access to finance

Country	Type of intervention	Year	Key findings on impact	Additional explanations
Uganda	Combining entrepreneurship training based on the ILO's Start and Improve Your Business programme (four days) with different forms of access to finance (loans and grants).	2012	<ul style="list-style-type: none"> ❑ Large effect on business performance for combination of loans and training¹ (profits of beneficiaries increase by 54 per cent as compared to control group), effect of loans only (initially 30 per cent) fades away quickly and is insignificant nine months after the intervention, grants only as well as grants and training do not show an impact on profits. ❑ Large employment effects, especially on family employment (66 per cent) but also for employees hired from outside the household (45 per cent). ❑ Some positive effects on capital accumulation (not significant). ❑ No effects on profits or employment for women-owned enterprises for any of the combinations offered. 	Randomized control trial offering four different packages (loan only, loan and training, grant only, grant and training), based on design, high credibility of results.
Viet Nam	Providing training on gender issues and business management based on the ILO's Get Ahead programme (nine modules of one hour, delivered over nine months plus additional weekly coaching) provided as a complement to micro loans.	2012	<ul style="list-style-type: none"> ❑ Considerable effects on business performance for women attending training with their husbands (profits increase by 26 per cent as compared to control group), positive effects for women attending the training alone (not significant).² ❑ Significant positive effects on business literacy, gender knowledge, new business practices (with or without attendance of husbands). ❑ Significant impact on women's empowerment as measured by women's belief of control over their lives, reduction of domestic violence by partners, and increased bargaining power of women (attendance of husbands only makes a difference for the last indicator). 	Randomized control trial at the level of 187 credit centres of the largest microfinance institution of North Viet Nam (TYM) offering the package of training and microcredits to: (1) women and their husbands with the aim of reducing potential intra-household conflicts; and (2) to women only, based on design, high credibility of results.

Country	Type of intervention	Year	Key findings on impact	Additional explanations
Ghana	Offering business management training based on the ILO's Improve Your Business programme (five days plus some tailor-made one-day modules) as an award for participating in a business plan competition (free scholarships).	2010	<ul style="list-style-type: none"> <input type="checkbox"/> No effect of the training on enterprise growth measured by sales, profits, investment, and number of paid employees.³ <p><i>Other results:</i></p> <ul style="list-style-type: none"> <input type="checkbox"/> Scores received from judges of the business plan competitions highly correlate with future enterprise growth. <input type="checkbox"/> Measuring abilities of enterprise owners through surveys (combination of years of formal schooling, numeracy, financial literacy, and non-verbal reasoning) is even stronger associated with enterprise growth. Access to credit and attitude measures (such as risk attitudes) are not related with enterprise growth. <input type="checkbox"/> Combining both measures is a stronger predictor of growth than either one alone. 	<p>Randomized control trial offering the scholarships to 50 per cent of the applicants of the business plan competition.</p> <p>The main research question was whether business plan competitions and testing enterprise owners' abilities and attitudes through surveys are an effective tool to identify growth-oriented enterprises. The training was an add-on to the experiment to provide an incentive for participation.</p>
Sri Lanka	Combining entrepreneurship training based on the ILO's Start and Improve Your Business programme (seven to nine days) with cash grants for existing and potential women-owned micro-enterprises.	2009	<p><i>For existing business owners:</i></p> <ul style="list-style-type: none"> <input type="checkbox"/> Improved business practices. <input type="checkbox"/> Improvement of business performance for combination of training and grants (short-term increase of profits that are up to 70 per cent higher than for control group, but effect fades away after one year; long-term increase of capital stock of 30 per cent), no effect of training only. <p><i>For potential business owners:</i></p> <ul style="list-style-type: none"> <input type="checkbox"/> Short-term effect on establishing a new business for both treatments (stronger for the training plus cash leading to a 29 per cent increase in the likelihood of opening a business as compared to control group), effect dissipates after one year. <input type="checkbox"/> Long-term effects on profits and sales for training only (approx. 40 per cent higher than in control group), no significant positive effects for training plus grants. 	Randomized control trial offering training only or training plus a cash grant to two groups of women (existing enterprises and potential start-ups), ⁴ based on design, high credibility of results.
Pakistan	Offering rural microfinance clients basic business training based on the ILO's Know About Business programme (eight days) and a loan lottery (seven times the average loan size = \$1,700).	2007–08	<ul style="list-style-type: none"> <input type="checkbox"/> Training leads to increased business knowledge. <input type="checkbox"/> No effects of training or training and loan on establishment of new businesses. <input type="checkbox"/> Training helps to improve business practices (for men only, 13 per cent as compared to control group). <input type="checkbox"/> Training leads to Increase in income (for men only, 7 per cent, package of training and loans does not perform better). <input type="checkbox"/> Lower business failure (for men only, -6 per cent). <input type="checkbox"/> Increase in child labour (school absence increases by 9 per cent, for male-owned businesses only). 	Random selection from microfinance clients of five branches of a Pakistani bank. ⁵

Country	Type of intervention	Year	Key findings on impact	Additional explanations
Ghana	15 days of management training for existing SMEs in metalworking cluster based on the ILO's Start and Improve Your Business programme.	2007	<ul style="list-style-type: none"> <input type="checkbox"/> Better business practices established (36 per cent of participants introduced bookkeeping compared with 6 per cent in control group). <input type="checkbox"/> Better business performance (only 10 per cent of participants report a reduction in sales and profits compared with 30 per cent in control group).⁶ <input type="checkbox"/> Higher probability of enterprise survival (8 per cent). <input type="checkbox"/> Employment effects not measured. <input type="checkbox"/> Strong cost/benefit ratio; benefits in terms of increased annual profits are 18 times higher than local cost of delivery. 	Randomized control trial offering training only, high credibility of results.
Tajikistan	Four-day management and gender training for women-owned start-ups based on the ILO's Get Ahead programme, as stand-alone and as combination of training plus loans.	2010	<ul style="list-style-type: none"> <input type="checkbox"/> Better business performance for those who take training and loans (number of beneficiaries reporting increased turnover increases by 68 per cent compared with no increase in control group), no effect for training only. <input type="checkbox"/> Positive employment effect for combination of training and loans (self-employment among beneficiaries increases 60 per cent compared with no increase in control group), no effect for training only. <input type="checkbox"/> Weak positive effect on registration, no effect on reinvestment of profits. <input type="checkbox"/> No impact on women economic empowerment (control over loans, savings, and expenses). 	Quasi-experiment, medium credibility of results as control group was matched based on client database of the microfinance institution implementing the experiment; matching methodology cannot fully eliminate differences between treatment and control group. ⁷
Philippines	Three-day basic management training for clients of a local microfinance institution based on the ILO's Start and Improve Your Business programme.	2010	<ul style="list-style-type: none"> <input type="checkbox"/> Improvement in self-assessed business skills. <input type="checkbox"/> Increased profits (monthly profits almost doubled). <input type="checkbox"/> Some positive effect on reducing over-indebtedness (late repayments decreased by 4 per cent) and multiple borrowing (taking a loan to repay another loan decreased by 10 per cent). <input type="checkbox"/> Some effects on risk management (5 per cent increase of microinsurances to cover unforeseen expenses). 	Quasi-experiment, medium credibility of results as control group was matched using clients of another branch with similar characteristics.

¹ All results listed are short- to medium-term effects. A new survey is currently being run to assess longer-term effects; see also: N. Fiala: *Stimulating microenterprise growth: Results from a loans, grants and training experiment in Uganda*, unpublished (2014).

² Vu et al.: *The impact of gender and business training for female microfinance clients in Vietnam*, unpublished (2014).

³ M. Fafchamps and C. Woodruff: *Identifying gazelles: Expert panels vs. surveys as a means to identify firms with rapid growth potential*, unpublished (2014).

⁴ S. De Mel, D. McKenzie and C. Woodruff: *Business training and female enterprise start-up, growth, and dynamics: Experimental evidence from Sri Lanka*, unpublished (2013).

⁵ X. Giné and G. Manzuri: *Money or ideas? A field experiment on constraints to entrepreneurship in rural Pakistan*, unpublished (2011).

⁶ This is a good illustration of why it is important to have an experimental design with a control group when doing impact assessments. Overall, all enterprises surveyed reported a reduction in sales and profits due to the massive competitive pressure from Chinese imports to Ghana. However, the training seems to help enterprises to reduce this negative external effect of increased competition from imports, meaning that the intervention had a significant positive impact. See Y. Mano et al.: "How can micro and small enterprises in sub-Saharan Africa become more productive? The impacts of experimental basic managerial training", in *World Development* (2012, Vol. 40, 3).

⁷ R. Gravesteyn: *Microfinance and women entrepreneurship: An impact assessment of a start-up loan program by IMON international (Tajikistan)*, ILO, unpublished (2012).

