

# **GLOBALISATION, STRUCTURAL ADJUSTMENT AND SMALL AND MICRO-SIZED ENTERPRISES IN MALAWI**

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By

**GERTRUDE ENNET MWANDUMBA**

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**Liverpool John Moores University**

**School of Social Science**

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## **ABSTRACT**

Globalisation and Structural Adjustment Policies (SAPs) have directly and indirectly impacted upon the performance of SMEs (Small and Micro-sized Enterprises) in developing countries. The SME sector is recognised to be playing a key economic role in employment creation, income generation and poverty alleviation. It offers opportunities for self-employment and has been noted to be offering some hope for the industrialisation process in developing countries. Globalisation and SAPs raise the problem of the ability of SMEs in developing countries to compete in a free market global economy. The main aim of this study was to analyse the impact of globalisation and SAPs on SMEs in Malawi through empirical investigation. A review of literature, which was undertaken as part of the study, formed the contextual framework for the empirical investigation. The literature revealed that globalisation offers the potential to raise economic growth rates and at the same time exposes firms and economies to intensive competitive pressures. It also revealed that global capitalism and market liberalisation as a condition of aid are part of the continued marginalisation of (sub-Saharan Africa) SSA. As well as SAPs being blamed for the problems experienced, other reasons which include poor infrastructure, small and fragmented markets, geography, natural resource endowments and poor information technology, have also been attributed to the industrial development failure and poor SME performance in SSA.

Analysis of the SAPs' impact was based on the perceptions of relevant government and non-governmental officers and business owners who responded to a questionnaire survey conducted on a sample of SMEs in Malawi. The survey revealed that trade liberalisation has exposed domestic firms to competition from imports before they are able to increase efficiency. The resultant floods of imports has reduced the market share of domestic SME production, and production for domestic market still remains much more important than exporting. The survey also revealed that, in general, Malawi lacks the physical and social infrastructure to support SME growth and trade liberalisation has not improved the performance of the manufacturing sector. Those SMEs with potential to grow and compete are constrained by lack of finance, high cost of inputs, lack of appropriate training programmes and technical capacity limitations. Malawi's economic growth and SME performance is also impeded by its landlocked status, dependence on a single cash crop for export and poor incentives for foreign and domestic investment. Thus, despite SAPs, Malawi does not seem to have succeeded in integrating into the global economy. The general consensus from this study is that the country is not well equipped to compete globally. There is lack of business skills and knowledge to recognise the opportunities and benefits of globalisation.

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## **ACRONYMS**

ADB/AfDB	Africa Development Bank
ADMARC	Agricultural Development and Marketing Corporation
AIDS	Acquired Immune Deficiency Syndrome
ARIA	Assessing Regional Integration in Africa
ASAC	Agricultural Sector Adjustment Credit
BEED	Business Expansion and Entrepreneurship Development
BoP	Balance of Payments
CEMAC	Central African Monetary and Economic Community
CGE	Computable-general Equilibrium
COMESA	Common Market for Eastern and Southern Africa
CSR	Centre for Social Research
DEMATT	Development of Malawian Traders Trust
DfID	Department for International Development
DTI	Department of Trade and Industry
EAC	East African Community
ECCAS	Economic Community for Central African States
ECfA	Economic Commission for Africa
ECOWAS	Economic Community of West African States
EDDRP	Entrepreneurship Development and Drought Recovery Programme
EFF	Extended Fund Facility
EIU	Economic Intelligence Unit
ESAF	Enhanced Structural Adjustment Facility
ESCOM	Electricity Supply Corporation of Malawi
EU	European Union
FAO	Food and Agriculture Organisation
FDI	Foreign Direct Investment
FRDP	Fiscal Restructuring and Deregulation Programme
G8	Group of Eight wealthy countries: United Kingdom, Russia, Germany, Japan, Italy, Canada, France and United States of America
GDP	Gross Domestic Product
GNP	Gross National Product
GATT	General Agreement on Tariffs and Trade
GEMINI	Growth and Equity through Micro-enterprise Investments and Institutions



HIPC	Heavily Indebted Poor Countries
HIV	Human Immunodeficiency Virus
IBRD	International Bank for Reconstruction and Development (also referred to as the World Bank)
ICT	Information Communication and Technology
IDA	International Development Association
IDC	Industrial Development Corporation
IMF	International Monetary Fund
ITPAC	Industrial and Trade Policy Adjustment Credit
LDCs	Least Developed Countries
MCI	Ministry of Commerce and Industry
MCP	Malawi Congress Party
MDC	Malawi Development Corporation
MDGs	Millennium Development Goals
MEPC	Malawi Export Promotion Council
MIPA	Malawi Investment Promotion Agency
MK	Malawi Kwacha (currency unit)
MNCs	Multi-National Companies
MPH	Make Poverty History
MPRSP	Malawi Poverty Reduction Strategy Paper
MSE	Micro and Small Enterprises
MVA	Manufacturing Value Added
NEC	National Economic Council
NGOs	non-governmental organisations
NSSA	National Sample Survey of Agriculture
NSO	National Statistical Office
OECD	Organisation for Economic Co-operation and Development
OPEC	Organisation of the Petroleum Exporting Countries
PAP	Poverty Alleviation Programme
PCL	Press Corporation Limited
PGL	Press Group Limited
PRGF	Poverty Reduction and Growth Facility
PRSP	Poverty Reduction Strategy Paper
PSIP	Public Sector Investment Programme

RA	Research Assistant
RER	Real Exchange Rate
SACU	Southern African Customs Union
SADC	South Africa Development Community
SALs	Structural Adjustment Loans
SAM	Social Accounting Matrix
SAP	Structural Adjustment Programme
SAPs	Structural Adjustment Policies
SECALs	Sectoral Adjustment Loans
SEDOM	Small Enterprise Development Organisation of Malawi
SMEs	Small and Micro-sized Enterprises
SMP	Staff Monitored Programme
SPS	Sanitary and Phytosanitary Standards
SSA	sub-Saharan Africa
TBT	Technical Barriers to Trade
TNC	Trans-national Corporation
UDF	United Democratic Front
UN	United Nations
UNCDF	United Nations Capital Development Fund
UNCTAD	United Nations Conference of Trade and Development
UNDP	United Nations Development Programme
UNICEF	United Nations International Children's Fund
UNIDO	United Nations Industrial Development Organisation
US/USA	United States of America
USAID	United States Agency International Development
WB	World Bank
WDI	World Development Indicators
WIDER	World Institute for Development Economics Research
WTO	World Trade Organisation

# **Chapter One**

## **General Introduction**

### **1.1 Aim**

The principal aim of this research was to analyse the impact of globalisation and Structural Adjustment Policies (SAPs) on Small and Micro-sized Enterprises (SMEs) in Malawi.

### **1.2 Objectives**

The research aim was achieved through the following objectives:

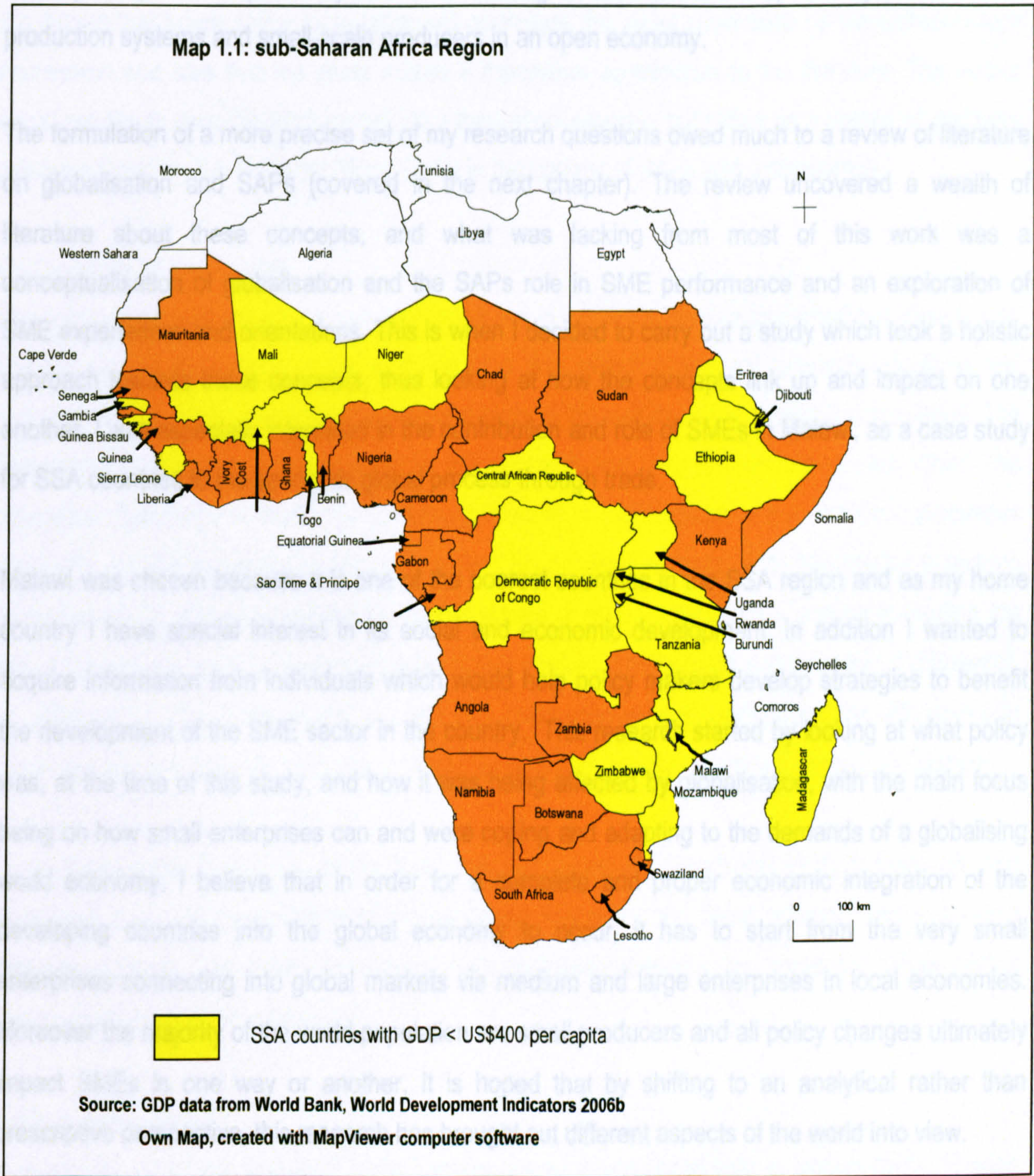
1. Assess the impact of Structural Adjustment Policies, in particular trade liberalisation, and consequences of globalisation on the small and micro-sized enterprise sector in Malawi
2. Analysis of the response of the SMEs to adjustment measures, thus, find out if the SMEs were becoming more competitive and efficient as predicted, in terms of export growth and increase in share of domestic market
3. Determine of the local production and distribution networks among the SMEs themselves and also with large enterprises and if free trade is creating opportunities for making new and profitable connections amongst the enterprises
4. Critically analyse the new economic environment of 'free trade' to see if it is suitable for the development and sustained growth of SMEs.

### **1.3 Purpose and Motivation of the Research**

There were both personal and academic reasons for carrying out this study. To begin with, the research was born out of my personal experience of living in a country which had adopted SAPs before becoming democratised. Soon after Malawi became a democratic country (1994), I observed some changes in the economic and social environment. As the nature of the political environment changed so did the business environment and attitudes towards small businesses. These observations sparked an interest in SMEs and in particular the problems and benefits posed by SAPs. The idea of this research began with the question: are SMEs in Malawi benefiting from SAPs and globalisation? This brought about a number of questions related to the complex interplay between globalisation, SAPs and SME experiences in a free market economy. I was curious about a specific phenomenon, which is the impact of globalisation and SAPs on SME performance in sub-Saharan Africa (SSA), in particular, Malawi. The term SSA has been used in this study to describe those countries of the African continent that are to the south of the Sahara desert. It contains many of the least developed countries in the world, with those regarded as the world's poorest, with less



than US\$400 per capita highlighted in the Map (Map 1.1). The main motivation for choosing the topic was personal interest in people, attitudes and institutions and special interest to investigate economic policies affecting lives of many people in a globalising world.



The study topic was also chosen because it links in with my academic background: in business and population studies and a special interest in socio-economic analysis. My personal aim was to understand globalisation and SAPs, in particular trade liberalisation and its impact on SMEs. SMEs, SAPs and Globalisation were 'hot' topics of the late 1980s and 1990s in the social and economic academic disciplines of development studies. There have been many studies, both theoretical and



empirical, that have been carried out in an attempt to determine the impact of globalisation and SAPs on economic development of SSA countries. In the past other studies have focused on a specific social or economic concept ranging from globalisation, SAPs to SME characteristics and development, with comparatively little work focusing on the internal and specific dynamics of local production systems and small-scale producers in an open economy.

The formulation of a more precise set of my research questions owed much to a review of literature on globalisation and SAPs (covered in the next chapter). The review uncovered a wealth of literature about these concepts, and what was lacking from most of this work was a conceptualisation of globalisation and the SAPs role in SME performance and an exploration of SME experiences and orientations. This is when I decided to carry out a study which took a holistic approach towards these concepts, thus looking at how the concepts link up and impact on one another. I was especially interested in the contribution and role of SMEs in Malawi, as a case study for SSA countries to the economic global process through trade.

Malawi was chosen because it is one of the poorest countries in the SSA region and as my home country I have special interest in its social and economic development. In addition I wanted to acquire information from individuals which would help policy makers develop strategies to benefit the development of the SME sector in the country. This research started by looking at what policy was, at the time of this study, and how it was being affected by globalisation, with the main focus being on how small enterprises can and were coping and adapting to the demands of a globalising world economy. I believe that in order for a complete and proper economic integration of the developing countries into the global economy to occur, it has to start from the very small enterprises connecting into global markets via medium and large enterprises in local economies. Moreover the majority of the world population are small producers and all policy changes ultimately impact SMEs in one way or another. It is hoped that by shifting to an analytical rather than prescriptive perspective, this research has brought out different aspects of the world into view.

As this research analyses how local producers in Malawi responded to a competitive environment brought about by free trade policies, it is hoped that an important outcome will be information which would enable SME policy-makers, support institutions and the SMEs to see themselves as entrepreneurs, gaining insight into skills and capacity required to achieve sustainable growth, achieve enhanced productivity and improve their competitiveness. In order to feed back the results of the study to relevant stakeholders, a summarised report will be distributed to government and



NGO participants of this study, who are also the individuals involved in national economic policy and strategy formulation. This report will also be made available to those entrepreneurs who expressed an interest in the results of the survey.

It is hoped that future policy formulation will assimilate the views expressed by the entrepreneurs themselves and also that the study makes a theoretical contribution to the literature. The author would not like to view this work merely as a theoretical exercise but rather as a means of resolving problems faced by sub-Saharan Africa SMEs in the context of SAPs and globalisation.

#### **1.4 Conceptual Framework**

This section presents the conceptual framework within which the study was carried out (Figure 1.1). The Conceptual Framework aided in developing and selecting relevant research questions and realistic methods, and in identifying potential threats to the validity of the research conclusions. The Framework highlights the main themes of this research and their relationship to each other. The conceptual framework is useful for discussing impacts of globalisation of the economic processes and SAPs on SMEs. Central to this work, is the "Free Trade" concept. With free market economy, "emphasis is on individual enterprise, on the virtues of market competition and on restricting the role of the state to what is required to ensure that markets can operate successfully..." (Ravenhill, ed. 2005: p20). The "Free Trade" concept has been used here to understand the differences in perceived and real benefits and costs of trade liberalisation to SSA countries, specifically Malawi.

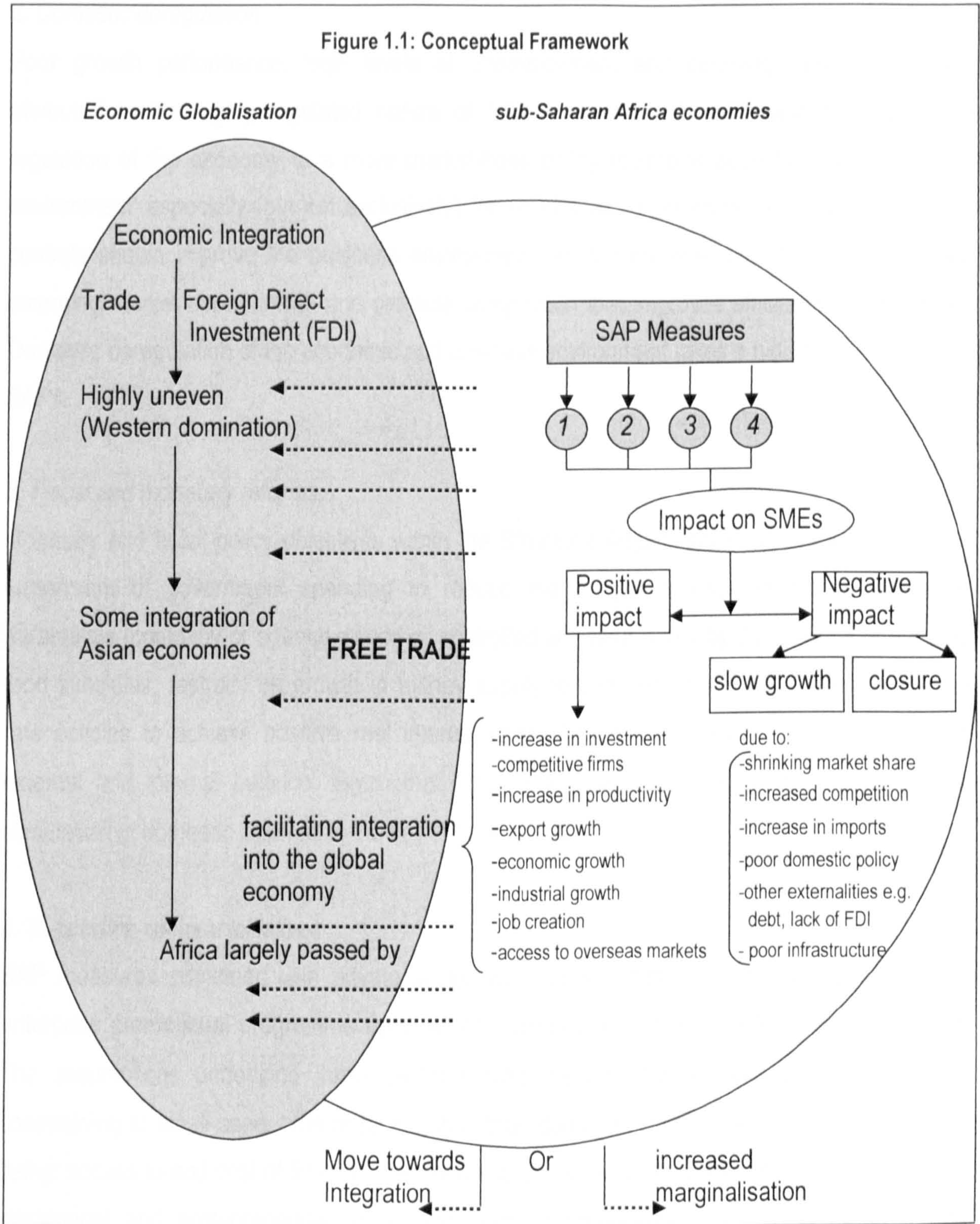
Trade liberalisation is just one of the four main SAP measures which this study focuses on. The others are domestic deregulation of the economy, monetary and fiscal reforms, and supporting sectoral initiatives. The main premises of each of these measures are presented below (World Development Report, several years).

##### ***1. Trade liberalisation***

In most SSA countries, non-tariff trade barriers played a prominent role in foreign trade. Foreign exchange allocation and import-licensing regulations were the key instruments used to effect import substitution. In addition to protecting domestic industries, these instruments endowed policymakers with power to direct scarce resources such as foreign exchange to areas targeted by government objectives. Trade policy reform has been central to the adjustment programmes supported by the World Bank (WB) loans and International Monetary Fund (IMF) programmes since the 1980s. It has been argued that, if trade barriers are removed, competition from abroad would force firms to cut



costs, improve quality and seek new ways of producing and selling their goods (World Bank 1987a).



The shift from import substitution to export orientation necessitates a change in foreign trade policy. As such, trade liberalisation assumes the most important place in debates on structural adjustment and it is intended to shift resources to the export producing sectors and away from those producing for the domestic market. The presumption is that trade liberalisation will raise the growth of exports and imports although the implications for the trade balance and balance of payments are uncertain



because this depends on the relative impact of liberalisation on export and import growth and prices of traded goods (Santos-Paulino and Thirlwall 2004).

## *2. Domestic deregulation*

Poor growth performance, high levels of unemployment and declining living standards are attributed to the highly regulated nature of SSA economies. A shift away from government regulation of the economy to a more market-base policy regime is seen to create an 'enabling environment' especially (but not exclusively) for small scale enterprises. Removal of government controls should improve the business environment, enable entrepreneurs to respond quickly to emerging market opportunities and promote competition that improves efficiency and productivity. Domestic deregulation of the economic and business environment takes a high profile in the Malawi SAPs.

## *3. Fiscal and monetary reforms*

Monetary and fiscal policy objectives within the Structural Adjustment Programme (SAP) include: curtailment of government spending to reduce the budget deficit; removal of subsidies to parastatals (company or agency owned or controlled wholly or partly by the government) including food subsidies; restraint on growth in money supply to curb inflation; market-determined interest rate policies to achieve positive real interest rates. These measures are intended to achieve external and internal balance. Given that small enterprises produce for the domestic market, stimulation of domestic incomes is the key to their growth.

## *4. Supporting sectoral initiatives*

SAP measures combined with private sector and donor initiatives, form the basis for a small enterprise promotional programme upon which government and donor efforts could be focused. The assumptions underlying these sectoral initiatives are that supply-side factors are more constraining to small-scale enterprise activities than demand-side factors. Supply-side constraints being: access to and cost of finance; a restrictive business and regulatory environment; inadequate managerial and entrepreneurial skills; and poor communication and infrastructure. If reform measures, which are supposed to help SMEs move from low-productivity informal sector to higher-productivity formal sector activities, are successfully implemented, they are likely to open up new economic activities for small enterprises. However, the size and relative isolation of SMEs have inhibited their ability to achieve economies of scale and they face tremendous difficulties in entering both national and global value chains driven by large trans-national corporations. These difficulties

coupled with other constraints, such as limited technical and managerial skills, insufficient knowledge with regards to laws and regulations and, more importantly, obtaining financing, urgently need to be overcome with specialist institutional support.

As presented in Figure 1.1, these measures, in particular trade liberalisation, were studied for their potential to integrate SSA into the global economy. These measures have been used to analyse the impact of the SAP on SME development in Malawi. The first three measures, when they were formulated, were not targeted at the SME sector, however, their impact has both a direct and indirect bearing on SMEs in Malawi (see section 2.6.2).

### **1.5 Summary and Chapter Outline**

The main aim of this research was to analyse the impact of SAPs and globalisation on SMEs in Malawi and to find out if the SMEs were becoming competitive in terms of export growth and see how they responded to changes in economic policy and reform measures prescribed by the IMF and World Bank. The rest of the thesis is organised as follows:

Chapter Two reviews Literature on globalisation and SAPs and impacts on sub-Saharan Africa and formed the analytical framework for the empirical work that followed. Literature review on economic and social consequences of globalisation at macro scale provided the contextual and theoretical framework within which the research on the study country was carried out. The chapter also provides up-to-date economic policy developments at international level which is intended to keep the readers informed of up-to-date economic policy changes and developments in the millennium years.

Chapter Three presents research methodology for the empirical work. Research techniques used are discussed and the techniques are fairly conventional social science tools: a combination of structured questionnaire and unstructured interviews designed to focus the research on the respondents' own experiences of the economic policy and global changes, and how they are impacting on them.

Chapter Four provides an overview of economic and political developments in Malawi from independence in 1964 through the initiation of the economic reform programme in 1981, through to the 1990s and more recent events of 2000s. It reviews the successful macroeconomic performance through to the mid-1970s and the subsequent macroeconomic downturn from the late 1970s which gave rise to the need for structural adjustment. Specific SAP measures applied in Malawi and



implications for the various economic sectors are also discussed here. Up-to-date information on Malawi economic situation is also presented.

Chapter Five focuses on SME sector development in Malawi. The Malawi industrial sector is presented and the development, role and distribution of SMEs are discussed in the context of the industrial sector. Underlying the discussion in this chapter are baseline survey results of work that was previously carried out in the past on the characteristics and dynamics of the SME sector in Malawi.

Chapter Six presents the survey findings. Empirical investigation of the research was carried out in two phases, and the chapter presents analysis of the findings from both phases. Responses to questions in a structured Questionnaire and to in-depth unstructured interviews were described and analysed. Analysis of the impact of globalisation and SAPs is also presented in this chapter. Characteristics of the enterprises and entrepreneurs have been discussed and the business operating environment analysed. Analysis of the impact of constraints and the regulatory environment has also been presented here.

Chapter Seven presents discussions of the research findings based on the primary research undertaken. Trade liberalisation, fiscal reform measures, domestic deregulation and globalisation are discussed in the context of the findings. Policy implications are also discussed in this chapter.

And finally, Chapter Eight presents overall conclusions on the study. The Chapter also discusses the direction of future research areas which could be further carried out. Personal reflections and final remarks are also presented in this Chapter.

## Chapter Two

### Theoretical Concepts and Literature Review

#### 2.1 Introduction

Alongside the process of globalisation, continues a process of marginalisation (which may be intrinsic to globalisation) of large parts of the developing countries from benefits of globalisation. Since the late 1980s, developing economies have been implementing economic policy reforms of the Structural Adjustment Programme. This research attempts to understand the dynamics of globalisation, including its promises and its potential pitfalls. Globalisation is not only creating remarkable opportunities for countries to enhance their development, it is also posing broad and complex policy challenges for governments, notable among them the proper handling of the costs of adjustment associated with trade liberalisation. The process of economic restructuring imposed by international creditors on developing countries since the beginning of the 1980s, and its consequences have also been discussed in this chapter.

The rest of the chapter is organised as follows: the second section discusses the concept of 'globalisation' as addressed in the literature, impact and implications of the economic globalisation process are also discussed; the third section discusses the concept of SAPs, beginning with a discussion of the nature of African economies in terms of economic historical origins, thus from colonial policies through import-substitution to neoliberal policies and the varying outcomes and consequences of SAPs; section four discusses economic performance of SSA since independence, SSA integration with the global economy, regional integration within SSA itself and effects of opening up and Foreign Direct Investment (FDI) are also discussed; section five sets the context of SMEs, manufacturing industry in SSA and discusses the impact of SAPs on the SME sector; section seven provides an up-date on recent developments in international policy changes; and the last section presents the chapter summary.

#### 2.2 The Concept of Globalisation

The concept of *globalisation* has gained considerable strength in recent years and its policy implications are not always clearly explained or understood. It radiates the possibility of a new analytical framework for domestic policy makers, and in some instances, the concerns of globalisation are motivated by the common good of humanity (Helleiner 2000). Some view globalisation as a process that is beneficial and key to future world economic development and also inevitable and irreversible. Others regard it with hostility, even fear, believing that it increases



inequality within and between nations, threatens employment and living standards and thwarts social progress. Walker and Fox (1996) said that the economic map of the world includes an increasingly integrated core, with pockets of local differences due to domestic intervention, and a large periphery of developing countries which, while dependent upon the core international market, are only loosely linked to it. Thus, the trend towards greater economic integration between nations is not universal.

### **2.2.1 Definition and driving forces of Globalisation**

The increasing integration of the world economies through a combination of capital, information and technology and trade flows has been referred to by some as *globalisation* (Hoogvelt 2001, Stein 1999). Baylis and Smith (2001) define *globalisation* as the process of increasing interconnectedness between societies such that one part of the world more and more have effects on peoples of societies far away. Some authors have defined *globalisation* as the shrinkage in space and in time that the world has experienced in consequence of the technological revolutions in transport, communication, and information processing (Hoogvelt 2001, Stein 1999). Dicken (2003), who says that Trans-national Corporation is arguably the most important single force creating global shifts in economic activity, and their strategies and operations are much influenced by the forces of technological change, also supports this definition. A distinction needs to be made between globalisation and internationalisation. Most authors agree that globalisation of economic activity is qualitatively different from the past trends of internationalisation. Dicken (2003) says that globalisation implies a much more advanced and complex form of internationalisation. The key feature, which underlies the concept of globalisation, is the erosion and irrelevance of national boundaries in markets which can truly be described as global (Hoogvelt 2001). From the extant literature, the main areas of change have been advances in and the fusion on information and technology and telecommunications; the rise of global business strategies and Trans-national Corporations (TNCs); new political economic structures; new political imperatives such as economic liberalisation; privatisation and deregulation; and the rise of the institutional investor (Dicken 2003, Hoogvelt 2001, Stein 1999).

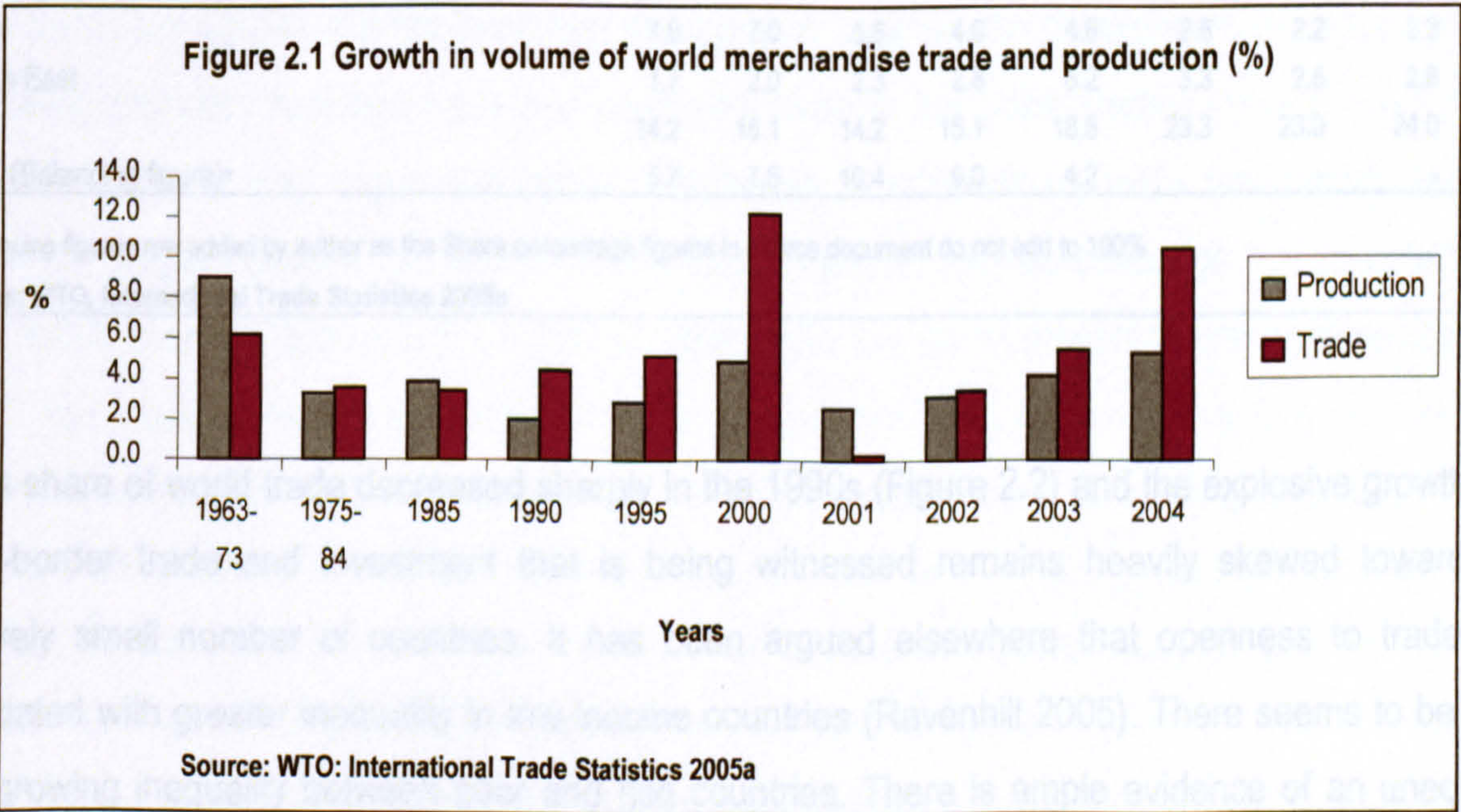
Several writers have distinguished three historical stages of globalisation (Marglin and Schor 1990, Ocampo and Martin 2003, Rodrik 2001b). The first stage identified is the period between 1870 and 1913 which is marked by a high degree of capital and labour mobility together with a trade boom that was a result of reduced transport costs rather than of free trade. The second stage was the period between 1945 and 1973. This period saw the disintegration of the macroeconomic regulation regime established in 1944 at Bretton Woods, first oil crisis, increasing mobility of private capital



and the end of the “golden age” (Marglin and Schor 1990). During this stage there were major efforts to develop international institutions for financial and trade cooperation and significant expansion of trade in manufacturers among industrial countries. The third stage of the globalisation process has been proposed to occur from 1973 onwards and has seen a gradual spread of free trade, governing presence of TNCs on the international scene, operating as internationally integrated production systems, expansion and mobility of capital, while at the same time imposing selective trade protection mechanisms and tight restrictions on the movement of labour. It is said that the third stage has been fuelled by successive technological revolutions and, most importantly, by advances that have cut the costs of transportation, information and communication. One of the major differences between the first and third stage of globalisation is that there is no corresponding liberalisation of labour flows, which are subject to strict regulation by national boundaries. Of all the stages of globalisation, this research focuses on the third stage, in particular, trade liberalisation.

**2.2.1.1 Economic integration, SSA and SMEs: an overview**

The first avenue of economic integration for most countries is intensifying international trade. Over the past 50 years, trade has been a major force driving economic growth. According to the World Trade Organisation (WTO), the volume of trade has grown consistently faster than the volume of world output since the 1950s (WTO 1996). In the 1990s alone, world trade grew at an annual average rate of 6.8%, more than double the annual world output average growth of 3.2% (WTO 2005a). World trade growth reached as high as 12% in 2000, one of the highest in the last decade (Figure 2.1). Years 2000 and 2004 were good for both global output and trade growth. In 2004 the expansion of world merchandise output and trade averaged 5.3% and 10.4% respectively. In fact, all regions reported faster economic growth in 2004.





Despite this impressive trend of growth in world trade over the years, with exports rising from US\$58 billion in 1948 to US\$8907 billion in 2004 (Table 2.1), Africa's trade performance has been of a downward trend since the 1960s. Its share of world exports fell from about 6% in 1963 to 3% in 2004 while imports fell from about 7% of world share in 1963 to 2% in 2004 compared to Asia which picked up considerably from the 1990s. In fact, Africa's share in world trade actually decreased sharply in the past decade (WTO 2005a) and its share in world exports fell from about 4.5% in 1983 to 2.6% in 2004 (Table 2.1).

**Table 2.1 Share of merchandise trade by selected regions and years (Billion dollars & percentage)**

	1948	1953	1963	1973	1983	1993	2003	2004
<b>Exports</b>								
	<b>Value (US\$ billion, current prices)</b>							
World	58.0	84.0	157.0	579.0	1838.0	3670.0	7342.0	8907.0
	<b>Share (%)</b>							
World	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
North America	28.3	24.9	19.9	17.3	16.8	18.0	15.8	14.9
South and Central America	11.4	9.8	6.3	4.3	4.4	3.0	2.9	3.1
Europe	31.5	34.9	41.4	45.4	43.5	45.4	46.1	45.3
Commonwealth of Independent States (CIS)	-	-	-	-	-	1.5	2.7	3.0
Africa	7.3	6.5	5.7	4.8	4.5	2.5	2.3	2.6
Middle East	2.0	2.7	3.2	4.1	6.8	3.4	4.1	4.3
Asia	13.6	13.1	12.4	14.9	19.1	26.2	26.1	26.8
Other (Balancing figure)*	5.9	8.1	11.1	9.2	4.9	-	-	-
<b>Imports</b>								
	<b>Value (US\$ billion, current prices)</b>							
World	66.0	84.0	163.0	589.0	1881.0	3768.0	7623.0	9250.0
	<b>Share (%)</b>							
World	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
North America	20.6	20.7	16.2	17.3	18.5	21.5	22.7	21.8
South and Central America	9.8	8.3	6.0	4.4	3.8	3.3	2.5	2.6
Europe	40.4	39.4	45.4	47.4	44.2	44.8	45.4	44.8
Commonwealth of Independent States (CIS)	-	-	-	-	-	1.2	1.7	1.9
Africa	7.6	7.0	5.5	4.0	4.6	2.6	2.2	2.3
Middle East	1.7	2.0	2.3	2.8	6.2	3.3	2.5	2.6
Asia	14.2	15.1	14.2	15.1	18.5	23.3	23.0	24.0
Other (Balancing figure)*	5.7	7.5	10.4	9.0	4.2	-	-	-

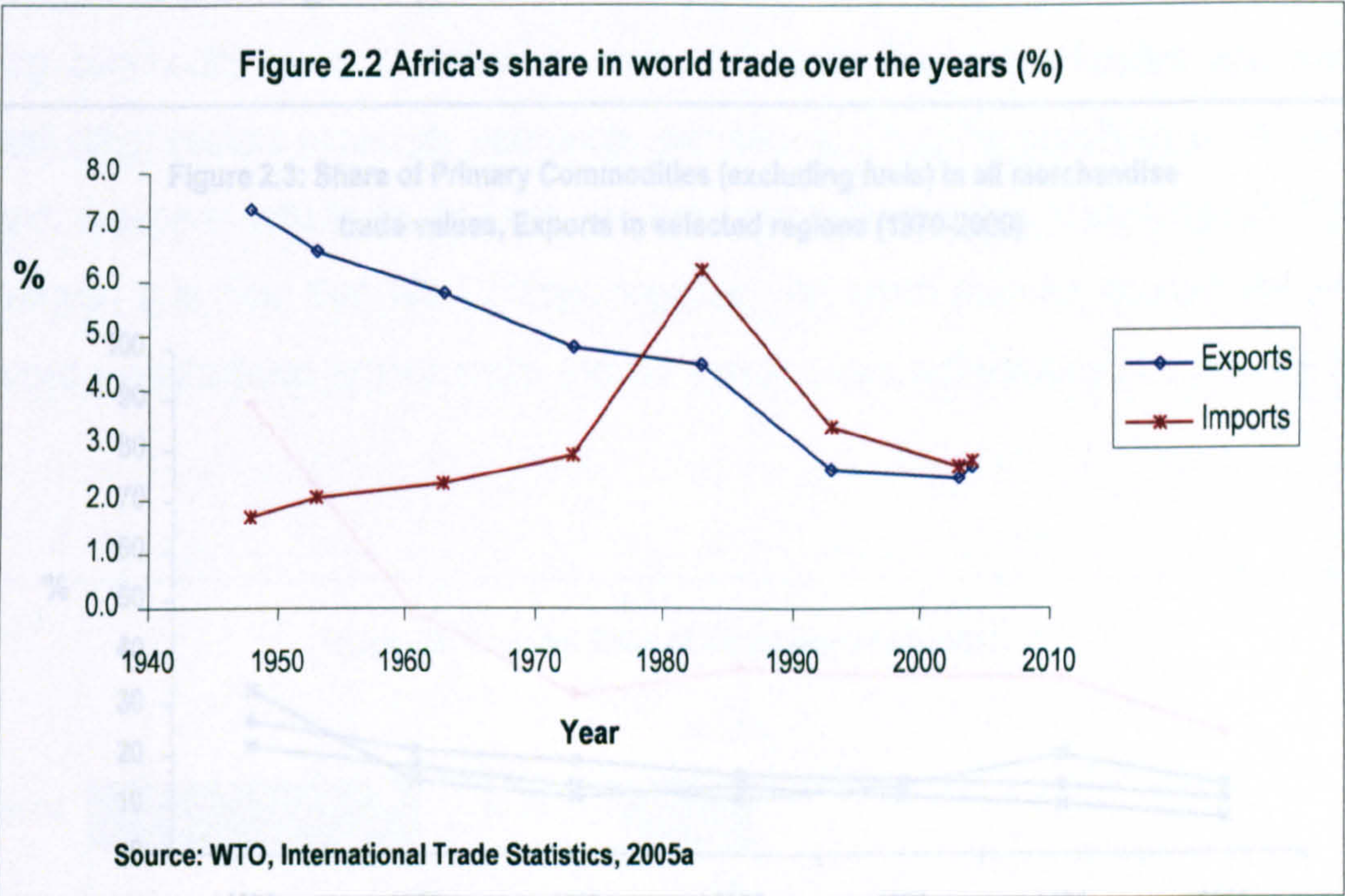
\* Balancing figures row added by author as the Share percentage figures in source document do not add to 100%

Source: WTO, International Trade Statistics 2005a

SSA's share of world trade decreased sharply in the 1990s (Figure 2.2) and the explosive growth in cross-border trade and investment that is being witnessed remains heavily skewed toward a relatively small number of countries. It has been argued elsewhere that openness to trade is associated with greater inequality in low-income countries (Ravenhill 2005). There seems to be an ever-growing inequality between poor and rich countries. There is ample evidence of an unequal



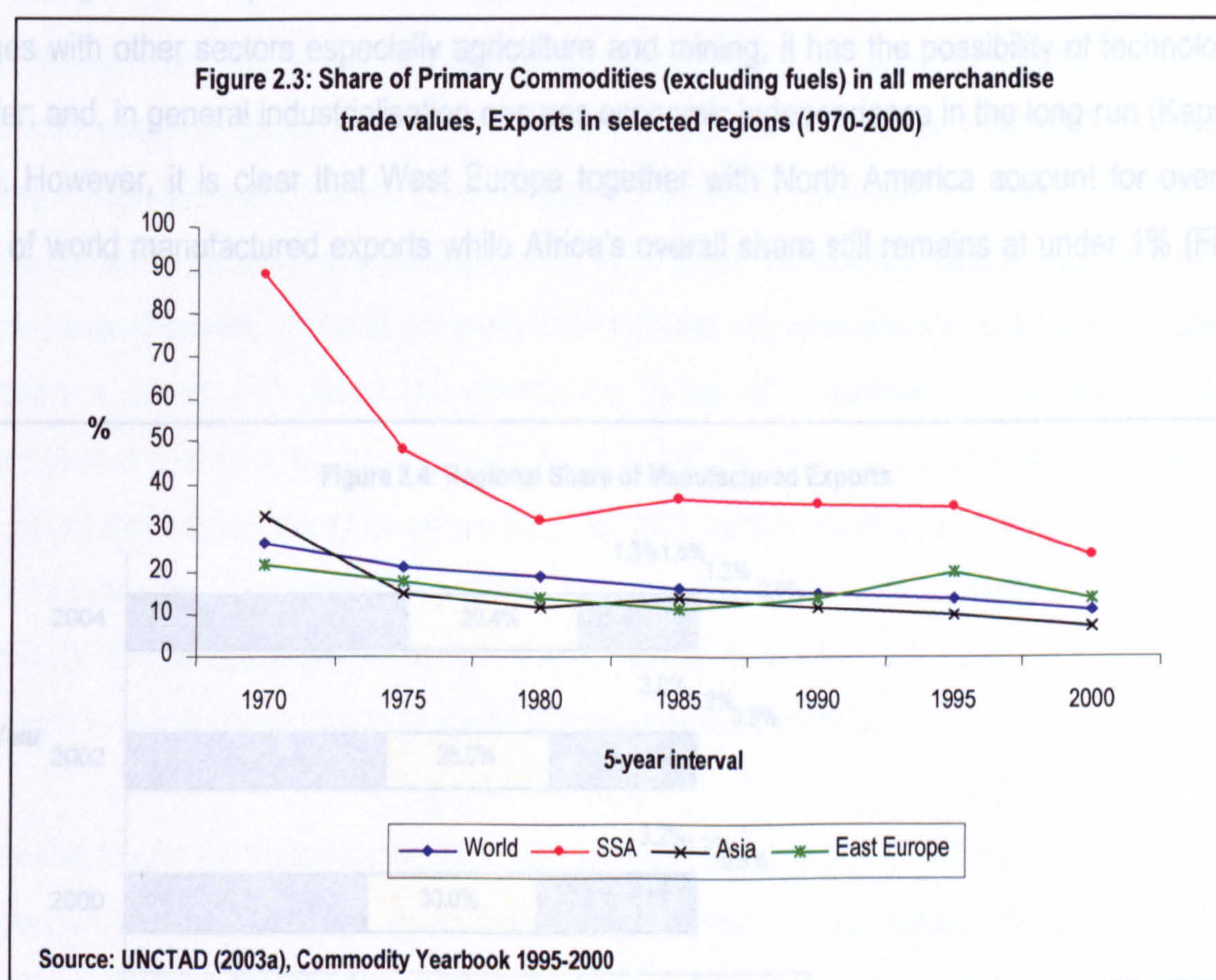
structure of trade, production and credit, which defines the role and position of developing countries in the global economy (Goldsmith and Mander 2001, Hoogvelt 2001). The United Nations Conference of Trade and Development (UNCTAD) attributed the decline in SSA's trade performance, to several factors which include general trends in global trade, the composition of Africa's merchandise trade, import-substitution trade policies, poor infrastructure, market access and agricultural policies in industrial countries and trade policies over the past 20 years (UNCTAD 2004). As pointed out by Collier (2000), the high transaction costs, such as transport and communication, renders the producers in the SSA region uncompetitive hence they are not well placed in the global economic system when they open their economies.



Dollar and Kraay (2004) attempt to answer the question on what can be expected to happen when developing countries liberalise trade and participate more in the global trading system. From their gathered evidence they argue that greater openness to international trade has contributed to narrowing the gap between rich and poor countries. However, they acknowledge that there will be some losers among the poor in the short-run, which effective social protection can ease so that all benefit from development in the long-run. Dollar and Kraay (2004) attribute other factors, such as poor transportation links within countries and the coast, that contribute to growing inequality rather than trade liberalisation. In their analysis they concluded that on average, greater globalisation is a force for poverty reduction. However, it has been argued elsewhere that, the playing field in international trade is not level as there still remain restrictions against imports of Africa's products (Oxfam 2005). Africa's trade is concentrated in a narrow range of primary commodities, and, within



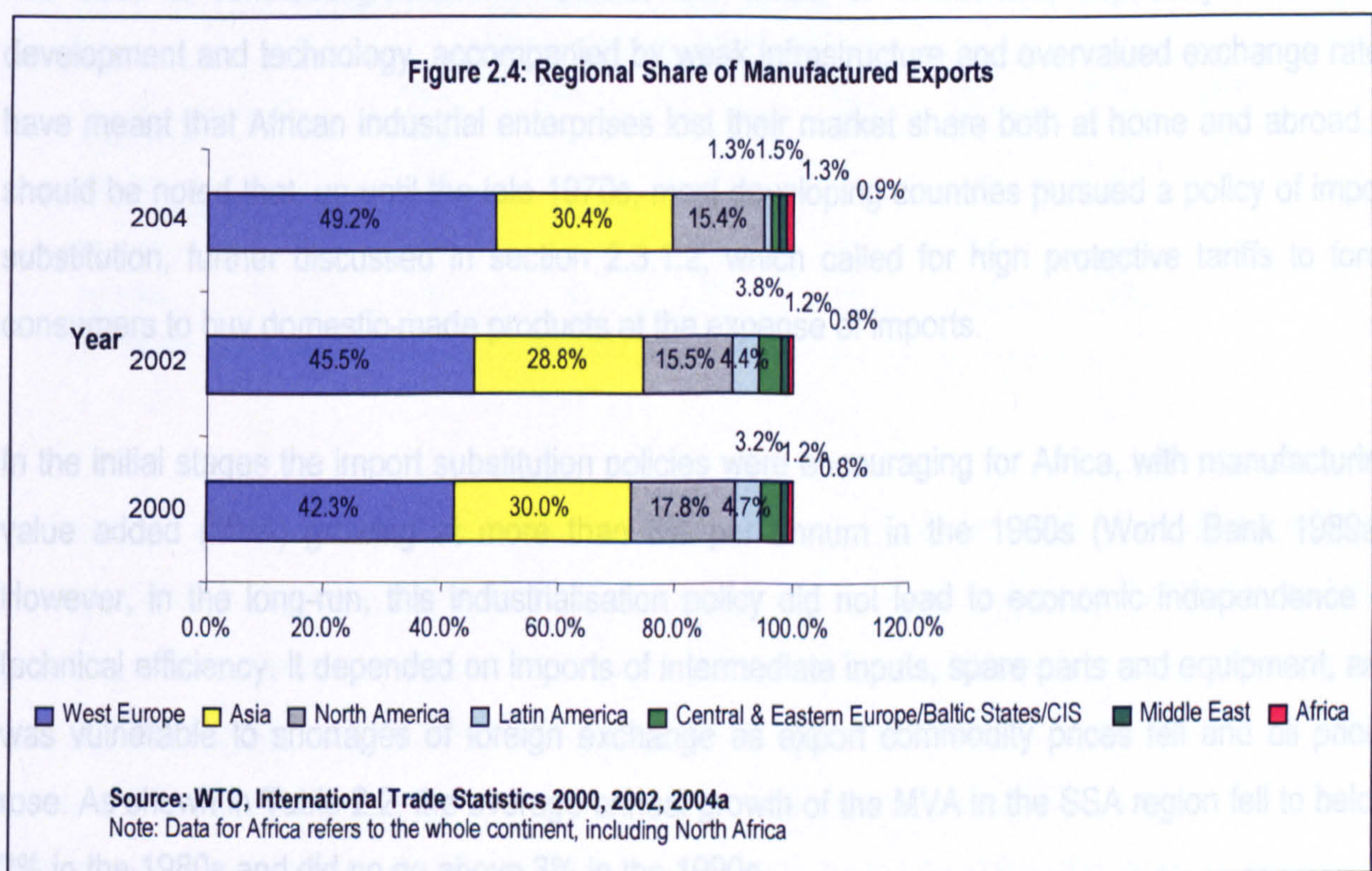
this narrow range, Africa's market share has been shrinking. The share of primary commodities in world exports such as food and raw materials, which are often produced by the poorest countries, has declined, and this reflects the overall downward trend in the world (Figure 2.3). For SSA the export share of primary commodities in all merchandise declined from 89% in 1970 to just 24% in 2000. Trade in primary commodities such as coffee, cocoa, cotton and sugar, for which most SSA countries depend on, has been sluggish, and an UNCTAD report revealed that SSA barely participates in trade in market-dynamic products (UNCTAD 2003a). While appreciating that agriculture is a very important economic sector for developing countries like Malawi, as this is traditionally the area in which they have enjoyed competitive trade advantages, it has been argued that the composition of what countries export is important and the strongest rise by far has been in the export of manufactured goods (UNCTAD 2003a).



Export of manufactured goods plays a very significant role in economic integration (IMF 2000). This view was acknowledged in a World Bank study, which reported that successful globalisers are those developing countries, which have managed to break into global markets for manufacturers and services and recognised that for many low-income countries, globalisation is not working (World Bank 2002a). Therefore due to lack of significant manufactured products, Africa has been missing out on the large expansion of international trade. Even recent indications are that Africa



has become ever more marginalised from trade at the global level over the past three decades, and that Africa's share of world exports has dropped by nearly 60% since the 1980s (WTO 2005a). In general, the world demand for export products of crucial export interest to SSA has been falling while heavy reliance on primary commodity exports has kept SSA vulnerable to market and weather conditions. Furthermore, most SSA countries have thriving informal manufacturing sectors that mostly meet local needs at low prices. For now, these countries may need to concentrate efforts on primary products, where they have a comparative advantage, but in the long run a shift towards promotion of manufacturing and export of manufacturing products may be required for Africa in order to achieve rapid productivity growth. The importance of manufacturing and industrialisation is widely being realised and it is considered to have several advantages over the primary sector development: industrialisation reduces risks and vulnerability to long-term deteriorating commodity terms of trade; the industrial sector has more forward and backward linkages with other sectors especially agriculture and mining; it has the possibility of technological transfer; and, in general industrialisation ensures economic independence in the long-run (Kapunda 2005). However, it is clear that West Europe together with North America account for over two thirds of world manufactured exports while Africa's overall share still remains at under 1% (Figure 2.4).



Although the total share of developing countries in world exports of manufacturers was around 35% in 2004, when the share is studied closely it is mainly the Asian economies which are doing well,



with 30% of total trade in 2004, whereas Africa as a whole fares poorly, at less than 1% in 2004. There is a general consensus that Africa's manufacturers are yet to make any significant inroads into the world markets. An explanation offered by Collier (2000) as to why Africa has had such a comparative disadvantage is that the policy environment in Africa is less conducive to efficient production than policy environment elsewhere. He argues that the policy environment has been particularly hostile to manufacturing activity and specifically singles out the policies which have the effect of raising transaction costs:

With high transaction costs, a transaction-intensive activity such as manufacturing is disadvantaged both absolutely and relative to the transactions-exports of agriculture and natural resources. This can be seen most dramatically in the context of very poor policy environments, which cause not just a decline in the economy but its reshaping away from transaction-intensive activities (Collier 2000: p19).

Collier argued that Africa has a productivity disadvantage in terms of location and capital endowment and poor policy environment. He points out that the cost of information is very high resulting in high transaction costs of manufacturing. However, it should be noted that there is no single explanation for SSA's low participation in world trade and country experiences have differed. In some, a rapid growth of import competition associated with globalisation and trade liberalisation has been a contributing factor. In others, low levels of investment, especially in skills in development and technology, accompanied by weak infrastructure and overvalued exchange rates have meant that African industrial enterprises lost their market share both at home and abroad. It should be noted that, up until the late 1970s, most developing countries pursued a policy of import substitution, further discussed in section 2.3.1.2, which called for high protective tariffs to force consumers to buy domestic-made products at the expense of imports.

In the initial stages the import substitution policies were encouraging for Africa, with manufacturing value added (MVA) growing at more than 8% per annum in the 1960s (World Bank 1989a). However, in the long-run, this industrialisation policy did not lead to economic independence or technical efficiency. It depended on imports of intermediate inputs, spare parts and equipment, and was vulnerable to shortages of foreign exchange as export commodity prices fell and oil prices rose. As shown in Table 2.2, the average annual growth of the MVA in the SSA region fell to below 2% in the 1980s and did not go above 3% in the 1990s.



<b>Table 2.2: Average annual growth in Manufacturers Value Added (%)</b>				
	<b>1980-85</b>	<b>1985-90</b>	<b>1990-95</b>	<b>1995-00</b>
Industrial countries	2.0	2.9	1.3	2.8
Europe & Central Asia	2.7	0.6	-11.1	4.2
sub-Saharan Africa	1.9	1.8	0.1	2.6
Latin America & Caribbean	-0.3	1.0	1.9	3.0
Middle East & North Africa	6.4	4.4	4.0	4.6
South Asia	6.6	7.6	7.0	4.8
East Asia	7.8	9.3	11.3	7.7
<b>Source: World Bank, World Development Indicators 2004a</b>				

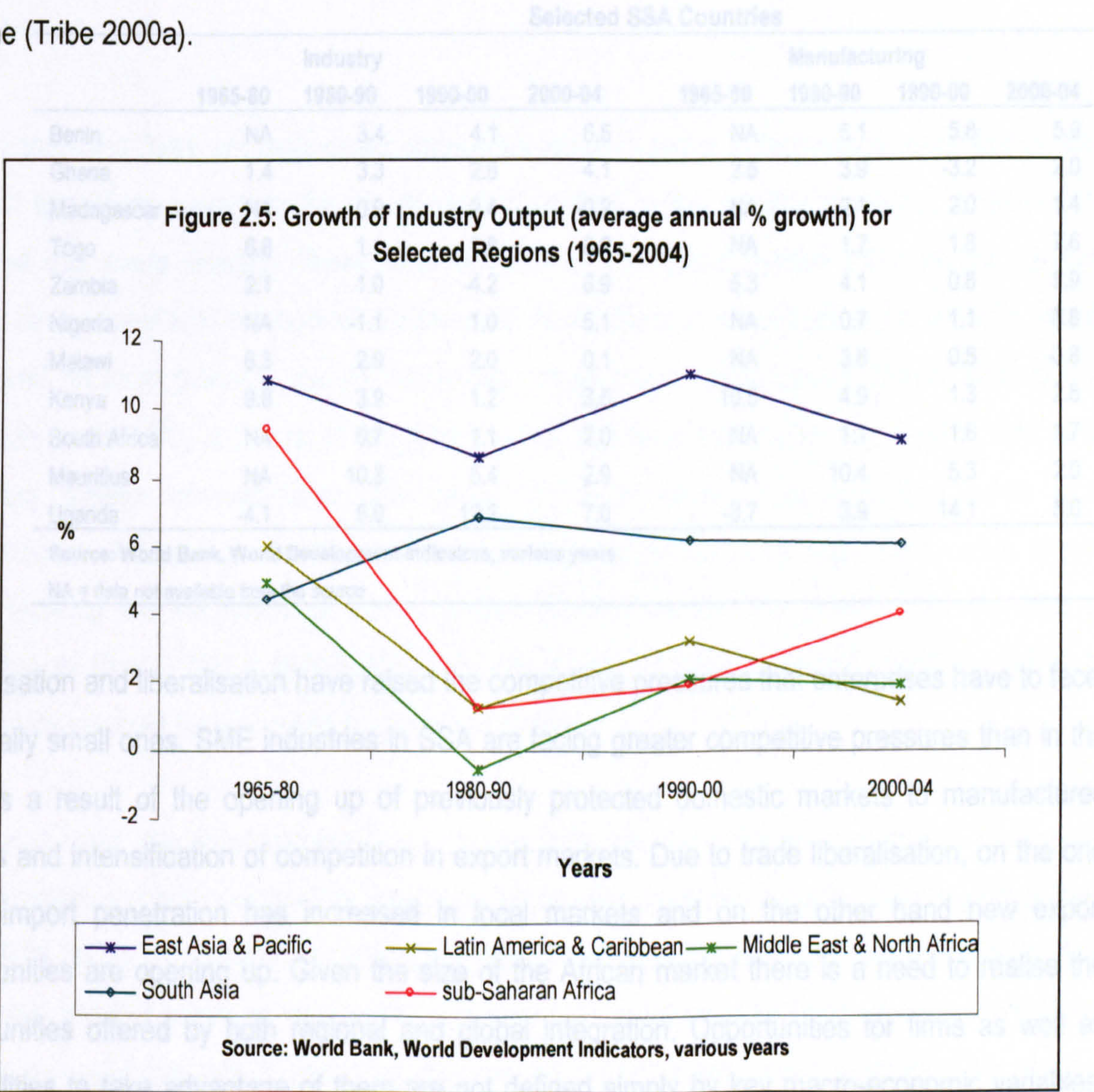
SSA's structure of output value added as a percentage of Growth Domestic Product (GDP) has hardly changed at more or less on a range of 12% to 15% between 2000 and 2005 (Table 2.3). However, as pointed out by Tribe (2002), interpretation of statistics relating to development of manufacturing sectors is difficult, and should be treated with caution, due to the fact that some agricultural and mineral exports contain a significant amount of manufactured value added, which may not be reflected in the industry value added figures.

<b>Table 2.3: Structure of Output for SSA Value Added as a % of GDP</b>							
	<b>1990</b>	<b>2000</b>	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>
Agriculture	19	17	15	18	17	16	14
Industry	34	30	29	29	31	32	39
of which							
Manufacturing	17	14	13	15	14	15	12
Services	47	53	57	54	52	52	47
<b>Source: World Bank, World Development Report, various years</b>							

For SSA as a whole, the industry output grew at 9.4% between 1965 and 1980, dropped considerably to 1.2% in the 1980s and only started picking up again in the late 1990s (Figure 2.5). From this picture it could be argued that most manufactured products, which are demanded by the international markets, were already being produced in great quantities by South and East Asian economies which were experiencing more rapid trade growth than SSA during the 1990s. Furthermore, the neighbouring SSA countries which could have been potential export markets may have been producing similar products so that there was even more competition amongst themselves. Growth through increase in export-manufacturing might have been already too late for



SSA manufacturers and primary commodities by themselves have not been enough to promote the kind of growth as that is being experienced by the newly industrialised countries of South East Asia. It should be noted that there is considerable variations in industrial characteristics among countries within the SSA region itself such that the decline in manufacturing output (referred to as de-industrialisation) is not even. Thus, there is a great diversity within the continent, with some countries falling in the 'newly industrialised countries' and others having very small manufacturing sectors, all growing at varying rates (Tribe 2002). For example in Ghana and Uganda, manufacturing output grew, as opposed to decline, from 2.5% and -3.7% (1965-80) respectively to 3.9% (1980-90) in both cases; whereas that of Kenya dropped from 10.5% to 4.9% during the same periods (Table 2.4). However, it has been noted elsewhere that there has been very substantial positive industrial development in SSA as a whole over the last 15-20 years, and others, Uganda and Ghana for instance, have experienced a substantial recovery from a period of economic decline (Tribe 2000a).



Africa's manufacturing sector is not competitive due to: lack of policy which promotes technological capacities or specific knowledge needed to enhance efficiency; lack of policies which encourage



innovation and economies of scale leading to technologically inefficient firms; high transaction costs which include high tariff and non-tariff barriers, high internal transport costs, poor telephone systems, and unreliable infrastructure facilities for essentials like water and electricity. While there are some dynamic enterprises in Africa, the vast majority fail to link into sources of dynamic industrial growth, rendering them uncompetitive within the open market economy. In order for the SMEs to benefit from the opportunities which come with an open market economy it also depends to a greater extent on what the SME can create, manage and produce. The business environment in which the SMEs operate is also governed by a number of other factors which include financial and legal regulatory frameworks, overall macroeconomic policies, industrial strategy and policy, availability of access to factors of production and infrastructure.

Table 2.4: Growth of Output (average annual % growth)								
Selected SSA Countries								
	Industry				Manufacturing			
	1965-80	1980-90	1990-00	2000-04	1965-80	1980-90	1990-00	2000-04
Benin	NA	3.4	4.1	6.5	NA	5.1	5.8	5.9
Ghana	1.4	3.3	2.6	4.1	2.5	3.9	-3.2	2.0
Madagascar	NA	0.9	2.4	-0.2	NA	2.1	2.0	1.4
Togo	6.8	1.1	1.8	8.2	NA	1.7	1.8	7.6
Zambia	2.1	1.0	-4.2	8.9	5.3	4.1	0.8	5.9
Nigeria	NA	-1.1	1.0	5.1	NA	0.7	1.1	8.8
Malawi	6.3	2.9	2.0	0.1	NA	3.6	0.5	-0.8
Kenya	9.8	3.9	1.2	3.5	10.5	4.9	1.3	2.5
South Africa	NA	0.7	1.1	2.0	NA	1.1	1.6	1.7
Mauritius	NA	10.3	5.4	2.9	NA	10.4	5.3	2.0
Uganda	-4.1	5.0	12.2	7.0	-3.7	3.9	14.1	5.0

Source: World Bank, World Development Indicators, various years

NA = data not available from the source

Globalisation and liberalisation have raised the competitive pressures that enterprises have to face, especially small ones. SME industries in SSA are facing greater competitive pressures than in the past as a result of the opening up of previously protected domestic markets to manufactured imports and intensification of competition in export markets. Due to trade liberalisation, on the one hand, import penetration has increased in local markets and on the other hand new export opportunities are opening up. Given the size of the African market there is a need to realise the opportunities offered by both regional and global integration. Opportunities for firms as well as possibilities to take advantage of them are not defined simply by key macro-economic variables, but also depend on how the firms are inserted in both local and regional production and distribution networks. For Africa's manufacturing SMEs, that are oriented towards the local market and are uncompetitive, increased inter-firm linkage can be the first step towards closer integration with the

world economy. Existence of inter-firm linkages between enterprises as a result of subcontracting as well as other forms of networking and co-operation within an area is termed 'clustering' and it has been argued that 'clustering' contributes to the capacity of SMEs to compete (Pyke and Sengenberger 1992, Schmitz 1992).

Most of the industrial enterprises in Africa can be characterised as small or, more frequently, micro. The 'missing middle' between large enterprises and small informal manufacturing activities is arguably the root cause of the lack of forward and backward linkages in Africa. Micro-enterprises employ only a handful of workers, who are often family members or relatives. Such micro enterprises in many respects are more like household activities. Survival rates are low and these small and micro enterprises rarely graduate into the formal sector. Therefore there is a need for collective efficiency through horizontal integration and organisational and technological links with large firms.

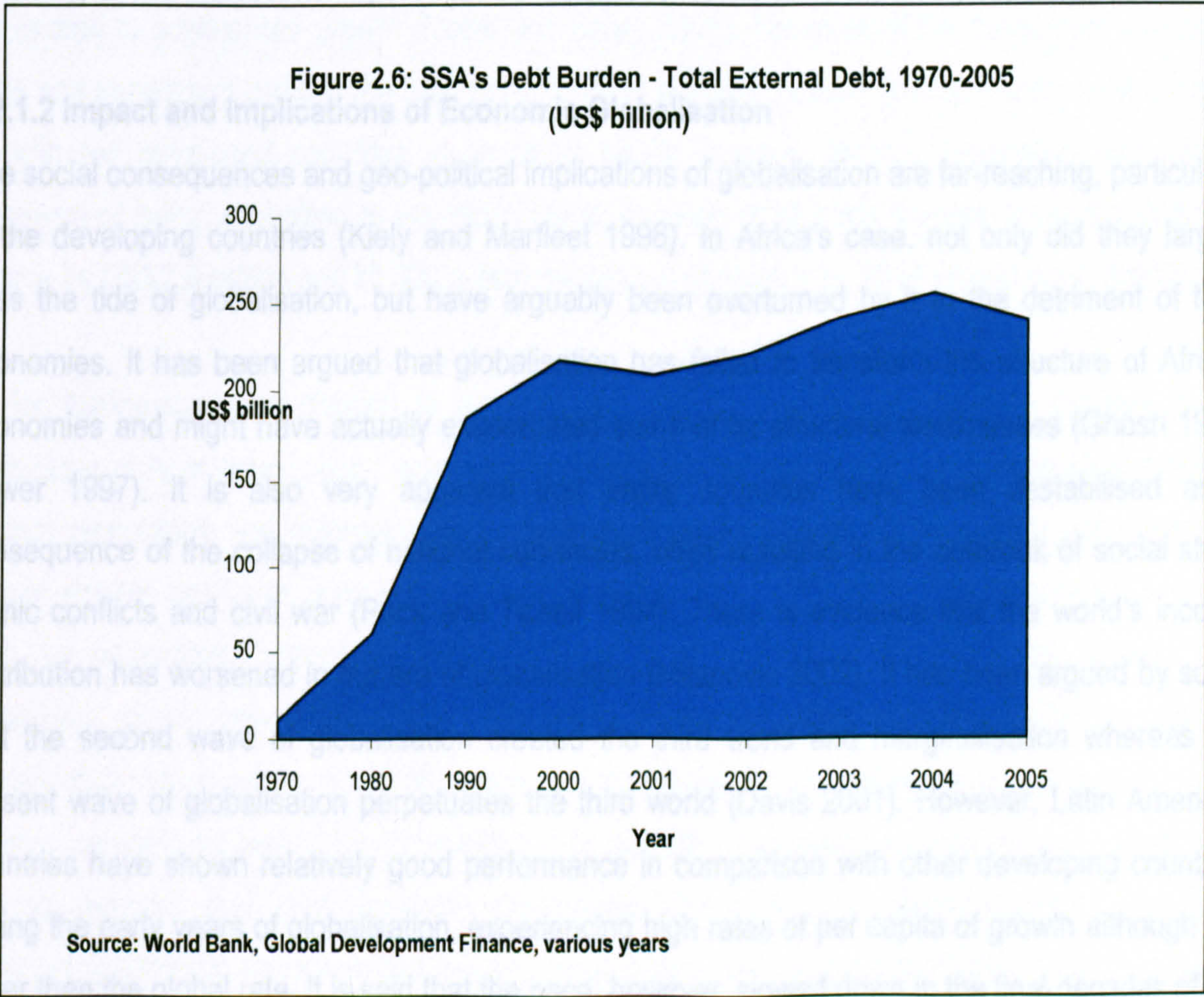
On the one hand there are large-scale enterprises which in terms of technology, organisation and scale of operations belong to the global system centred in the wealthy North but spreading its tentacles into every country. These local outposts of the global system often produce export commodities of one kind or another. On the other hand, there is a multitude of local SMEs, which are based on local markets, usually producing simple consumption goods, formal training and education matter little, and most of the units involved are fairly small. They are local in the sense that their system characteristics are based on local needs, resources and other local circumstances. A presence of network connections between these global and local systems should surely facilitate the integration of SSA countries like Malawi into the global economic system. According to Cho (1994) subcontracting systems which continue local and traditional forms of organisations should be connected to global corporations.

It has also been argued elsewhere that entrepreneurs use networks as a source of information about markets and technologies that they hope will provide them with a competitive edge over their rivals (Barr 2002). Information on technology, output markets standards and how markets function does have a direct effect on productivity and may help entrepreneurs become more competitive and improve output quality. In theory, entrepreneurial networks are meant to facilitate the process of economic growth by helping the entrepreneur capture of knowledge externalities which may be used in conjunction with the other factors of capital and labour, say, in the production process (Barr 1995). Data from Ghanaian manufacturing sector suggested that networks are potentially very



important in determining economic outcomes (Barr 1995). Thus, the networks can affect enterprise performance by providing entrepreneurs with information about the world especially technologies which will have a direct effect on its productivity, and about markets, how they function and standards which to comply to, which would help enterprises become more competitive.

As well as the marginalisation of SSA countries being reflected in their small share of world trade, output and foreign investment, and uncompetitive enterprises, it is also exacerbated by Africa's unstable external debt. In 1970 total external debt for SSA stood at US\$11billion and by 2003 it had gone up twenty one fold to US\$231billion (Figure 2.6). The external debt owed declined by small amounts between 2000 and 2002, probably due to the Heavily Indebted Poor Country initiative relief, which was launched in 1996 (further discussed in section 2.6), when some countries reached a decision point and had begun to get their debt relief in phases.



However, it can be seen that in general the debt burden does not seem to have declined over the past years, reflecting poor performance in economic activity growth. Despite the cash injections provided by the loans, no indebted African country has sincerely prospered and any prospects of reduce and mitigate risks it generates. They argue that it reflects poverty because more investment



economic recovery and growth is being sacrificed by servicing of debt. Recent developments on the issue of debt are further discussed in section 2.6.

Economic globalisation is of considerable importance now, such that regulators and policy makers need to be aware of its various implications, and any policy suggestions need to be applied within its context. Government policy is now influenced and dictated by the free and massive flow of capital worldwide. It has been contended that those countries with an open market approach are said to be more likely to prosper in the global economy as capital, both human and financial, increasingly ignores national boundaries (Krueger 1998). Some argue that greater openness and interdependence between national economies provides wonderful opportunities for poorer countries, but also challenges, as most of the poor countries are still feeling marginalised by globalisation (Milanovic 2002). The following section discusses some of the debates within the literature, on the impact and implications of economic globalisation, especially with regards to SSA.

#### **2.2.1.2 Impact and implications of Economic Globalisation**

The social consequences and geo-political implications of globalisation are far-reaching, particularly in the developing countries (Kiely and Marfleet 1998). In Africa's case, not only did they largely miss the tide of globalisation, but have arguably been overturned by it to the detriment of their economies. It has been argued that globalisation has failed to transform the structure of African economies and might have actually exacerbated some of its structural weaknesses (Ghosh 1999, Power 1997). It is also very apparent that entire countries have been destabilised as a consequence of the collapse of national currencies, often resulting in the outbreak of social strife, ethnic conflicts and civil war (Peck and Tickell 1994). There is evidence that the world's income distribution has worsened in the era of globalisation (Milanovic 2002). It has been argued by some that the second wave of globalisation created the third world and marginalisation whereas the present wave of globalisation perpetuates the third world (Davis 2001). However, Latin American countries have shown relatively good performance in comparison with other developing countries during the early years of globalisation, experiencing high rates of per capita growth although still lower than the global rate. It is said that the pace, however, slowed down in the final decades of the 20<sup>th</sup> Century (Ocampo and Martin 2003).

Collier and Dollar (2002) have assessed the impact of globalisation and proposed an agenda for action to enhance the potentials of globalisation and provide opportunities for poor people and to reduce and mitigate risks it generates. They argue that it reduces poverty because more integrated



economies grow faster, and this view is supported by Kiggundu (2002b) who argues that globalisation offers the poor and oppressed the best hope, opportunity and propensity to get out and stay out of poverty and to enjoy freedom. He argues that support for economic globalisation is based on the realisation that it enables nations, governments, societies, enterprises and individuals to create more wealth and generate more income through more efficient modes of production, consumption and exchange. Dollar and Kray (2004) argued that greater openness accelerates GDP growth performance and does not increase income inequality within countries but that trade liberalisation impacts favourably on growth. The key challenge for the developing countries is therefore to create and sustain an enabling environment for the development and competitive performance of the productive sectors, and strengthen their manufactured export base.

Trade and investment are at the heart of globalisation and it has been argued that trade goes hand in hand with faster growth (Lindert and Williamson 2001). Both increased trade and increased FDI are related to accelerated growth (Dollar and Kraay 2001). For most of the developing countries, trade and investment provide the best opportunity to alleviate poverty among citizens and to catch up with the developed countries in terms of wealth creation, income generation and raising standards of living. According to the World Bank, abolition of all trade barriers would boost global income by US\$2.8 trillion and lift 300 million people out of poverty by 2015 (World Bank 2001).

As for businesses, globalisation is an important emerging business mandate relevant to all businesses. It is an Information Economy, as opposed to an Industrial Economy business concept. Modern technology and communication enable businesses to operate in multiple countries with diverse shapes and forms of organisation and control (Teece 1986). In addition, innovation in areas such as computing, telecommunications, financial services and transport has lowered the transaction costs associated with conducting commerce across international boundaries. Globalisation raises many practical issues and concerns for the individual business enterprise. Foreign competition inside home markets has steadily increased, as has foreign investment through mergers and joint ventures. Companies are looking to global markets and even undertaking dramatic reorganisation to become globally more competitive (Porter 1998b). Against the backdrop of growing competition and globalisation, countries are increasingly concerned about how conducive their business environments are to private investment and business development and how they stand regionally or globally (Batra et al. 2003).

Globalisation has also brought out anxieties from other angles. For the developing countries there are anxieties about being shut out of markets, distant investors coming in, being uncompetitive,



environmental degradation, social dislocation and international imbalances in power. There are also anxieties about globalisation in rich countries though different in nature: terrorism, inequalities within rich countries, loss of manufacturing jobs to low-wage countries, being some of them. There are also global anxieties such as global inequality, thus, the richer getting richer whereas the poor are getting poorer, global warming, power of governments, labour and capital. Dicken (2004) argues that it is important to recognise that globalisation cannot be regarded as a causal factor in development rather within the umbrella notion of globalisation there are particular processes which will have certain place and time-specific context. He argues that the same process can have very different impacts both spatially and in relation to diverse groups of people. It has also been argued elsewhere that globalisation should not be viewed as a reliable substitute for a domestic development strategy (Sanchez 2003). Sanchez says that policy makers need to design and implement an active development strategy not only to benefit from, but also to help counteract the negative effects of the immutable forces of globalisation. Thus, they need to pursue both active liberalisation and active domestic development policies. Another concern voiced by critics of globalisation, is that in today's increasingly interdependent global economy, economic power is shifting away from national governments towards supranational organisations such as the WTO, the European Union (EU), and the United Nations (Kuttner 1996).

### **2.3 The Concept of Structural Adjustment Programme**

The concept of Structural Adjustment Programme was a response to the economic crisis of SSA in the 1970s and was introduced specifically to tackle structural and macro-policy problems in Africa. It is a process by which the IMF and WB base their lending to developing economies on certain conditions, pre-determined by these institutions in order to meet its long-term needs of efficient utilisation of factors of production to ensure sustained growth and hence be able to repay the debts owed to these institutions (Woodward 1992). Therefore, from the beginning of the 1980s, IMF and WB prescribed economic policies under "structural adjustment programme", which was a condition for developing countries obtaining new loans from multilateral institutions. Countries, which refused to accept the Fund's corrective policy measures, faced serious difficulties in rescheduling their debt and/or obtaining new development loans and international assistance.

The main elements in adjustment programmes have centred round the following objectives: strengthening Balance of Payments (BoP) position; reduction in domestic financial imbalances, including less government deficit financing; elimination of price distortions in various sectors of the economy; promotion of domestic savings in public and private sectors; domestic deregulation and



trade liberalisation and thereby improving export levels. These policies generally follow from an economic philosophy of 'neo-liberalism'. This ideology claims that the market is the most efficient mechanism for the distribution of goods and services in society, that private property and capitalist economic principles are the most efficient means for production of goods, and that state interference with the working of the market and capitalist production should be minimised.

The results have been a series of measures including dramatic waves of privatisation, a reduction in the state's role in economic planning and policy making, and often dramatic cuts in government-supplied social services in accordance with the dictates of structural adjustment packages. Some analysts see the developing countries' debt crisis of the 1980s as a critical turning point in global economic relations (McMichael 2000). McMichael argues that the debt crisis created the objective conditions, institutional basis, political instruments, and ideas necessary to steamroller the poorer countries into accepting the neoliberal consensus on the value of trade liberalisation and fiscal discipline. Neoliberalism thus provides the ideological basis for globalisation, while SAPs provide the policy mechanisms for creating an economic context at the national level conducive to globalisation.

Before discussing the impact of the SAPs, it is thought important to present the context within which the adjustment measures were applied. Therefore, a brief historical background, the nature of African economies and Africa's economic performance since the 1960s is presented in the following sections.

### **2.3.1 Historical context of SSA Economies**

Most SSA countries are small, poor and open economies with a rapidly growing population of 514 million in 1990 to 725 million in 2004 at an average growth rate of 2.5% during that period (World Bank 2006b). A large number of the population in SSA live and work in the rural sector, poverty in all its dimensions is widespread, and living conditions are extremely difficult. World Development Indicators (2004a) showed that poverty rates had been falling in all regions except SSA in 2001. The latest available data showed that the share of people living on US\$1 per day was 44% for SSA in 2002 compared to 31% for South Asia and 11% for East Asia & Pacific (World Bank 2006b). Although, overall, extreme poverty in developing countries fell from 40% in 1981 to 28% in 1990 and 19% in 2002, SSA's share still remains above 40% (Figure 2.8). It has been estimated that more than 600 million people will still be trapped in poverty in 2015, most of them in SSA and South Asia (World Bank 2006b). Human resources are still critically underdeveloped, and lack of



institutional capability is also rampant. Production, which is severely affected by an array of human, physical, infrastructural and technological constraints, including the vagaries of weather conditions, is largely in the primary sector. Commercial activities are crucially dependent on imported factor inputs, and exports are based on only a few, mainly primary, export commodities.

In order to set the context and understand the present position of SSA economies, one must backtrack as far back as to the colonial era. Effects of colonialism should not be underestimated because one way or another, colonialism impacted on African economies and trade. It has been argued that this is still happening today through neo-colonial power relations that continue to exploit poorer countries and regions for the material benefit of their wealthier counterparts (Ashcroft et al. 1995). In this study, three distinctive periods have been identified with regards to historical policy analysis context: the colonial period; first decades of independence; and the more recent era of macroeconomic adjustment. The following sub-sections discuss the policies and their effects within each of these distinctive periods. Colonial policies are briefly discussed and their impact on small industries of African economies with main arguments given in the context of Malawi. This is followed by a brief discussion of import-substitution and post-colonial policies which were adopted during the first decades of becoming independent. Lastly, African economic performance since independence through to the years of macroeconomic structural adjustment policies is discussed.

#### **2.3.1.1 SSA and the Colonial era**

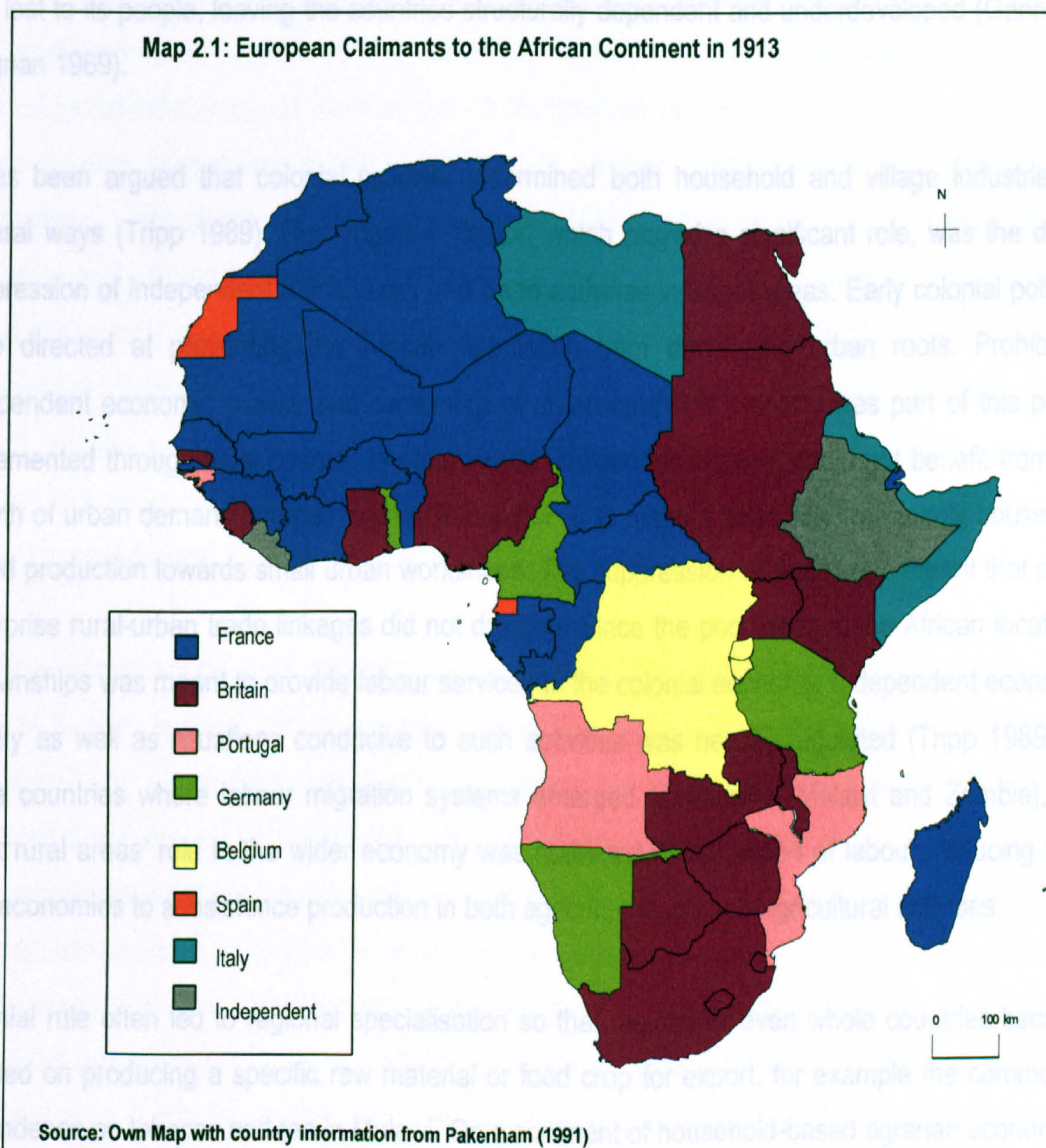
It has been reported that pre-colonial Africa included small family groups of hunter-gatherers, larger, more structured groups and heavily structured clan groups, whose trade network extended as far as China (Walter 1973). In 1482 the Portuguese established the first of many trading stations along the coast of Ghana with chief commodities being gold, ivory, spices and slaves. The European discovery of America in 1492 led to great development of the slave trade, in the coastal regions of Africa, which was phased out in Europe and America from the early nineteenth century. From mid-19<sup>th</sup> Century European explorers became interested in exploring the heart of Africa and opening the area for trade, mining and other commercial exploitations. By the end of the century the continent was well explored leading to the way for colonisation which followed. In the late-19<sup>th</sup> Century European powers occupied most of Africa, creating many colonial nation states leaving only two independent nations: Liberia and Ethiopia (Map 2.1).

1885 to 1945 was a period of high imperialism with several kinds of colonial organisation. For instance in Kenya and Zimbabwe, which were white settler colonies, established an elite caste system with master-slave relationship between the white and black and the whites expropriating



vast areas of the best farmland. The degree of colonisation differed from state to state. Other colonisers were limited to small numbers of administrators, traders and missionaries. Direct rule colonies (Senegal, as an example) and indirect rule colonies, such as Nigeria and Botswana, relied heavily on traditional African rulers. Colonial regimes devoted only the resources needed to provide the minimum infrastructure and social services to accomplish this end. Schooling, health and related social services were restricted to those segments of the population deemed potentially beneficial to the European capitalists. Only 5% of Africans were allowed to be educated in missionary schools and it is believed that they received the western-style education not to become leaders of their own countries, but to assume subordinate positions in the colonial system. Removal of the hub of political power from the local population undermined the authority of the kinship system. All welfare activities were directed to meeting the interests of the non-indigenous populations and these alone (MacPherson 1982).

**Map 2.1: European Claimants to the African Continent in 1913**





European motives were to acquire and control new markets and obtain raw materials from Africa. They established an export economy that extracted raw materials and returned manufactured goods. Governments ensured an adequate supply of labour for European enterprises through the introduction of taxation schemes and this made it necessary for Africans to seek employment to earn the cash they needed to pay the taxes. Trade was oriented towards the Metropolis and this economic activity developed at the expense of indigenous populations. It often forced indigenous people into wage labour, their land was expropriated, they could not compete with the large commercial white farms and it created a dependency which in most countries still persists. European powers took advantage of the military and technological weakness of Africa to exploit the mineral and agricultural wealth. The incentive for colonialists was to expropriate rents as quickly as possible rather than think of the long-run. As a result of lack of political control by Africans and systematic expatriation of wealth, African countries became producers of an economic value that was lost to its people, leaving the countries structurally dependent and underdeveloped (Gann and Duignan 1969).

It has been argued that colonial policies undermined both household and village industries in several ways (Tripp 1989). One important factor, which played a significant role, was the direct suppression of independent artisan craft and trade activities in urban areas. Early colonial policies were directed at preventing the African population from developing urban roots. Prohibiting independent economic activity and ownership of urban land and property was part of this policy implemented through local council. In other words, indigenous artisans could not benefit from the growth of urban demand in order to grow in number or to make a transition from purely household based production towards small urban workshops. The suppression of retail trade meant that small enterprise rural-urban trade linkages did not develop. Since the population in the African locations or townships was meant to provide labour services to the colonial economy, independent economic activity as well as situations conducive to such activities was heavily regulated (Tripp 1989). In those countries where labour migration systems emerged (Zimbabwe, Malawi and Zambia), the black rural areas' role in the wider economy was restricted to the export of labour, reducing their own economies to subsistence production in both agricultural and non-agricultural activities.

Colonial rule often led to regional specialisation so that regions or even whole countries became focused on producing a specific raw material or food crop for export, for example the commodity dependence on tobacco and tea in Malawi. On a continent of household-based agrarian economies with very little long-distance trade, colonialism imposed cash-crop production for export, and



mineral-extraction, with manufacturing supposed to come later. Africa was colonised for exploitation and the aim was to maximise their resources. For instance, local people were encouraged to grow cotton to keep the cotton mills of England going, not to enrich Africans. Colonial governments formulated philosophies and policies in relation to native, labour and land, and these policies had effects on Africa (Gann and Duignan 1959, Hailey 1938). Least productive part of land was left to the Africans and the rest was taken by the European settlers and people were ordered (forced labour) to cultivate economic crops which Europeans relied on (Gann and Duignan 1959). It can be said that colonialism left a legacy in most of Africa, as economic life still largely revolves around agricultural cycle that remains acutely dependent on capacious weather conditions. International flows of people, capital investment, aid and debt repayments also continue to reflect past colonial ties (Ashcroft et al. 1998).

#### **2.3.1.2 First decades of independence: import-substitution through to neoliberal policies**

The colonial occupation continued after the end of World War II when all colonial states gradually obtained formal independence. As discussed in the previous section, colonial state structures were geared towards expanding export production of taxable primary crops and minerals. At independence, African governments inherited this policy and were relying on peasant export production and mineral production for revenue and growth. New leaders relied on rural notables, whose allegiances were secured through the chains of patronage stretching from the Ministers' offices to the villages. It was, however, realised that this system was not working as there was not enough patronage to go around and unmanageable opposition by the excluded was growing. Centralised bureaucratic regimes were then created in which an all-powerful President controlled patronage systems with the help of a central bureaucracy and army (Allen 1995).

The development efforts were geared towards structural transformation. Governments were on a spree of building schools, clinics and other physical amenities, all under stringent state control. However, these governments were still expected to earn their revenues as primary product exporters. Surpluses accumulated from agricultural sector were to be applied to infrastructure and other requirements of import-substitution driven industrialisation. Backed by rapid economic growth and nationalisation of a foreign-dominated private sector, massive investments were made in infrastructure, from road construction to new import-substitution enterprises which were handed over to the parastatal sector. As regards to industry, the newly independent African governments often assumed a control-oriented policy since the industries established by white settlers were monopolistic or oligopolistic in nature. Through administrative measures, foreign exchange



allocation, investment regulation and the like, governments gained considerable control. Lack of trust, sometimes combined with politicians' and bureaucrats' lack of familiarity with mass-manufacturing industry, and with political constraints of dealing with minorities, created a restrictive business environment rather than a supportive government industrialisation policy (Riddell 1990). In some cases where the expatriate community left at the time of independence, this led to a virtual collapse of industries. Africanisation of economic activity took place to a significant degree in many countries, but often primarily in farming, trade, transport, and real estate. In manufacturing industry, however, this process was much slower and in many countries not very extensive (Ettema 1987). The policy to industrial development in the 1960s and 1970s in Africa was of Import-substitution (IS). IS relates to 'infant industry' (newly established activities) promotion concept and this generally involves factory mass-production of consumer goods. Import-substitution policies (applied both before and after independence) were directed toward protecting domestic factory producers from competing imports through tariffs or quantity restrictions. And as foreign exchange became more and more scarce, policies followed which increasingly regulated foreign exchange allocation to licensed producers, thereby increasing barriers to entry by small industrialists and traders.

The high priority given to industry implied a relative neglect of agriculture, often accentuated by worsening terms of trade for agriculture resulting from price and taxation policies. Oshikoya and Mlambo (2002) argued that the favouring of industry meant discriminating against agriculture, even though the agricultural sector was the main employer as well as the dominant exporter in most African countries. It is believed that the manner in which policies of import-substitution were pursued in most SSA countries from the 1960s to the 1980s left a legacy of inefficient industries, as well as missed opportunities as many industries, which lacked sufficient local markets, exhibited low levels of capacity utilisation, and lacked motivation to seek out external markets (Belshaw and Livingstone 2002). It has been argued that import-substitution industrialisation in most African countries did not develop into more advanced stages due to the relatively small size of the domestic markets (Riddell 1990). As a result, monopolistic and oligopolistic market structure emerged with a few large enterprises, some of them nationalised after independence. It can be said that although during the colonial period the spread of industrialisation to African enterprises was deliberately repressed, the import-substitution did not stimulate small enterprise development either, as it remained concentrated in a few manufacturing units, heavily dependent on imports and with little inducement to learn and spread economic opportunity.



Although soon after gaining independence most SSA countries experienced economic growth, the 1970s, growing debt of the 1970s hit the continent, provoking acute financial distress, aggravated by declines in export earnings due to fall in commodity prices and oil curtailment by the Organisation for the Petroleum Exporting Countries (OPEC) which led to the global crisis in 1974. During that period, terms of trade for African agricultural products declined and loans from both public and private sectors advanced with crippling high interest rates. All the development efforts came to a stop as governments struggled economically. Furthermore, SSA economic backwardness discouraged any great influx of private capital flows from abroad. As a result, Africa became the most indebted area in the world with total external debt rising from 40% in 1980 to 79% in 1994 (Castells 1998).

Production in the industrial sector, which had shown much progress in the earlier two decades, grew little from 1980, and agricultural output could not keep pace with population growth. SSA's food production per capita which stood at 90% in 1980, declined to 84% in 1990 (FAO 1995). Recent indications are that production only started to recover in the 2000s reaching up to 90% in 2003 but still growing at a slower pace than population growth (FAO 2006). Daily per caput calorie supply in 1988 was at around 2000 calories, equivalent to the level of 1965, which is far below minimum nutritional requirements. Consequently, hunger and malnutrition became widespread (World Bank 1989d). The energy supply was at around 2207 calories in 2002 (FAO 2006). Decontrol of food prices, removal of consumer subsidies and increasing unemployment, especially since the 1980s have all weakened the purchasing power of Africa's consumers. They simply cannot afford to buy food for a normal and healthy life. In turn malnutrition and under-nutrition reduce people's ability to work by draining them of energy hence further perpetuates poverty.

The World Bank attributed "structural" factors as the root cause of the economic stagnation in Africa experienced during the 1970s. The World Bank singled out poor domestic policies as the main factor, in aggravating Africa's economic crisis during this period. Such policies were cited as overhauled currencies, heavy government spending and inward-looking trade policy (Husain and Faruquee 1994). The World Bank (1989c) suggested that the origins of the problems in the industrial sector in SSA could be traced back to high levels of protection and to the erroneous perception that development is equivalent to industrial growth. Lopes (1994) pointed out that the internal structural problems and the external factors impeding African economic growth were exacerbated by domestic policy inadequacies and a new approach for development in Africa was



sought. The industrialisation dream and money lent to support this was replaced by "neoliberalism" and this saw the end of "the development state" strategy.

Neoliberalism was revived in the early 1980s after Margaret Thatcher was elected to the British government and Ronald Reagan in the United States of America (USA), as they were strong proponents of it. Neoliberalism and other mainstream development frameworks draw their conceptual roots from neo-classical theory. The neo-classic theory uses profit and utility maximisation as core behavioural assumptions and the general equilibrium of competitive markets as an example of a well-functioning economy (Schumpeter 1954). The Neo-classical economics school of thought believes that free markets usually bring about an efficient allocation of resources, and that government interference will lead to an inefficient allocation of resources. Neo-classical economics underpins the theory of neoliberal development reform.

Neoliberalism, as neo-classical economics, sees markets as optimally efficient means of organising economies. State intervention is seen to disturb the natural tendency for competition, specialisation and trade to generate economic growth. Hence the neoliberal economic policies favour an outward-oriented, export economy, organised entirely through markets, along with privatisation, trade liberalisation and limited state budget deficits. This set of policies became the standard recipe, applied by global governance institutions to supplement countries regardless of national or cultural circumstances (Peet 2002). The main points of neoliberalism include: rule of the markets, thus greater openness to international trade, no price controls, total freedom of movement of capital, goods and services; cutting public expenditure; deregulation; and privatisation of state-owned enterprises. It should be noted that sometimes neoliberalism is used interchangeably with globalisation, especially when discussing global market liberalisation and free trade policies.

The neoliberal policies have also been referred to by some as the 'Washington Consensus', a term which was used by John Williamson in 1989 to refer to a list of ten policy recommendations for those countries willing to reform their economies (Williamson 1989). The ten policy prescriptions reflecting John Williamson's interpretation of the 'Washington Consensus' were: fiscal discipline; redirection of public expenditure; tax reform; financial liberalisation; adopting a single, competitive exchange rate; trade liberalisation; elimination of barriers to foreign direct investment; privatisation of state-owned enterprises; deregulating market entry and competition; and ensuring secure property rights. The 'Washington Consensus' was thought of as the lowest common denominator policy advice being addressed by the Washington-based institutions to Latin American countries as



of 1989 (Williamson 2000). Although the term 'Washington Consensus' is sometimes used interchangeably with the phrase 'neoliberal policies', John Williamson refutes it and says that the original interpretation was never to imply policies like capital account liberalisation, monetarism, supply-side economics or minimal-state intervention, which are all essential neoliberal ideas (Williamson 2000). Although the ten-point policy package was originally designed as a reform agenda for Latin America, it quickly became seen as a model for solving the problems faced by the wider developing world. It emphasised macroeconomic discipline (particular fiscal), a market economy and openness to the world economy, at least with respect to FDI. The neoliberal policies or the Washington Consensus were imposed on the developing world by the IMF and WB under the guise of structural adjustment.

The IMF and WB intervened on the problems faced by the developing countries by introducing a reorientation of economic policies, in particular in the form of stabilisation and SAPs. SSA countries had no choice but to comply as they were debtors after all. As already discussed, the essence of the approach to the SAPs was the 'neo-liberal' notion that States must divest themselves from direct participation in the economy and provision of social services to make way for free-market exchange. All barriers to trade including exchange controls, protective tariffs and public ownership had to be removed to allow for the operation of global market forces. Agriculture became key again as it was believed that this would stimulate the reassertion of the "comparative advantage" of rural Africa's cash crops within the global division of labour (Freund 1998). The WB and IMF were central to the process of dictating the global capitalism's new terms as they were the major creditors of SSA. It has been argued by some that this created a situation whereby SSA had parallel governments controlled by international lender agencies (Hutchful 1989).

It should be pointed out that the initial overall SAP objective was to deal with BoP problems and as a debt management strategy for developing countries. Later on this model was criticised for its inability to deliver promised economic growth and social impact as debt continued to mount (Cornia et al. 1987). In the 1990s, the IMF and the WB responded to the criticisms by offering some support in the form of micro-credit, social safety nets and social funds (Vivian 1995). However, attached to the support were 'conditions' which the countries had to adhere to in order to tap into the social funds. They included privatisation of public enterprises, domestic deregulation and liberalisation of trade. These have since been promoted as global development policies for SSA with trade liberalisation as an important element of the SAP. Green (1995) lists three stages of the SAP development policies:





These policies are based on the assumption that global economic integration through free trade is the most effective way to promote growth which would benefit society. However, it has been argued that policies like prior public expenditure cuts (in order to stabilise the economy) on infrastructure of transport links, institutional credit and small-farmer services could have the effect of reducing agricultural outputs, which are the dominant SME products in developing countries (Mosley et al. 1995). It has also been argued that trade liberalisation works better if industry is already competitive on export markets and privatisation works better if there is a private sector that is able and willing to take over the public sector's assets. Mosley et al. argued that infant industry in developing countries should have been protected:

The poorer the country, the more likely is such endogenous market failure (e.g. under-utilisation of productive land, inability of small business-men to borrow on commercial terms, lack of access to the market by producers of tradables ...) to constitute a constraint on production (Mosley et al. 1995: p311).

Thus, SMEs most under pressure from the competition of modern industry may not be in a good position to take advantage of the new opportunities which are being generated through economic integration. This may be because of deficient education, lack of knowledge of the new opportunities, lack of capital or simply because of locality. In order for SMEs to develop and graduate into significant industrial and commercial enterprises in a free market economy, they need to be competitive. The trade liberalisation policy could have been inappropriate to the economic context of SSA.



The following sections discuss the benefits and shortcomings of the major elements of the radical, comprehensive and innovative reform programmes, and the economic and social transition of developing countries during the era of the neo-liberal experiments of the SAP. It also reviews some of the theoretical arguments and empirical evidence in order to reach some conclusions on the question of the macro-impact of stabilisation and adjustment policies on poverty.

### **2.3.2 Consequences of SAP measures**

Malawi is one of the developing countries that adopted structure adjustment policy reform measures from the beginning of the 1980s (further discussed in Chapter Four), and specific measures taken as part of SAPs have directly and indirectly affected the development and performance of small and micro-sized enterprises in the country. The reforms, in the name of SAPs, concerned all economic sectors and notably the industrial sector which is called upon to play an increasing role as the state gradually withdraws from productive activities in favour of the private sector.

Due to the pervasiveness, dominance and prolonged nature of the stabilisation and adjustment policies, SAPs have had wide-ranging consequences, not only for the macro economy but also for incomes of the poor and for the social sectors. Under the SAP, demand-reducing policies, which include cuts in government expenditure, rises in taxation, reductions in real wages and credit restraint, are encouraged. These policies cut into real incomes by reducing employment and real wages of those in employment and raising prices of consumption goods, as prices are liberalised. Contraction of overall spending almost certainly lowers the well being of the poorest (Helleiner 1995). In his study of the impact of the 1980s adjustment on the poor, Samuel Morley, found that output per capita fell by over 10%, real value of the minimum wage fell by over 25%, and the numbers of the poor people rose by almost 20%. However, some countries (Columbia and Costa Rica) managed to both reduce poverty and improve distribution of income during the 1980s (Morley 1992, Morley and Alvarez 1992). Columbia avoided a recession during its stabilisation and adjustment period; even though its growth was not as rapid as in previous decades, it reduced both poverty and inequality. These results stand in stark contrast to the experience of almost every other country in Latin America. Some analysts have emphasised the part played by openness and export orientation as the main variables affecting growth and that lack of social capital and deficient political institutions have been the main proximate causes of slow growth (Azam et al. 2002).

There are conflicting hypotheses regarding effects of adjustment on poverty. Reviews of IMF programmes conducted by staff members concluded that in general, Fund programmes have



improved rather than worsened income distribution (IMF 1986). This view is supported by Srinivasan who argued that adjustment measures, by eliminating imbalances and attaining a sustainable and efficient development path, are likely to have a positive impact on the welfare of the poor (Srinivasan 1988). It has also been argued that the SAP has not had a negative impact on the poor, contrary to widespread perceptions (Sahn 1994). In a study on the impact of trade policy reforms in Cameroon, Gambia, Ghana, Malawi, Madagascar, Mozambique, Niger, Tanzania, and Zaire, Sahn concluded that there was no evidence that these programmes harmed the poor. And he contends that, in fact, the evidence shows that the poor had benefited in countries that fully adopted adjustment programmes.

This view is supported by Sharer (1999) who also contends that many SSA countries have made substantial progress with economic reforms in the 1980s. However, Sharer points out that in order to raise living standards and lift their populations out of poverty, African economies will need to grow faster than they are currently doing. In contrast, some analysts have expressed concerns over problems stemming largely from the falling wage share associated with currency devaluation (Pastor 1987, Taylor 1983). Others have argued that the effects will depend on the nature of the economy, and on the policy package adopted (Bourgignon and Morrisson 1992, Demery and Addinon 1987). It has been argued that growth of income per capita has been limited and after a decade of reform policies little if any has been achieved to reduce poverty (Morley 1995).

Most markets of developing countries have been significantly liberalised and this has drastically changed the structure of domestic demand in favour of imports, which have made big inroads into their markets and eroded the viability of domestic manufactures. It has been widely documented in literature that greater trade and financial integration of the developing countries has resulted in the worsening of their BoP position and domestic economic growth (Ghosh 1999, Hoogvelt 2001, Stein 1999). Rodrik (1997b) argued that inadequate implementation of reforms and policy reversals have contributed to the low credibility of African reforms, which negatively affect the desired response in investments and exports. A World Bank report pointed out that trade taxes are still higher in Africa than other developing regions and that anti-export biases continue to prevail in most countries (World Bank 2001). The report also points out that trade liberalisation has not gone far enough or locked onto a specific objective, such as the expansion of exports.

One of the measures for effectiveness of the SAPs is Gross Domestic Product growth (World Bank 1994), and a large part of most of the SSA countries' GDP is derived from the agricultural sector,



within which most SMEs predominate, and is the most dominant source of SSA export earnings. The SAP policy objectives did not include industrialisation strategy other than trade liberalisation. In the past, industrialisation strategy in most African countries discriminated against SMEs and, today, where technology and organisational competence is lacking, trade liberalisation efforts that abruptly remove protection may only cause a drop in manufacturing outputs. As SMEs are dominant in these countries, this thesis attempts to explore to what extent the SAP policies, in particular trade liberalisation, have impacted upon and supported the development of the SME sectors.

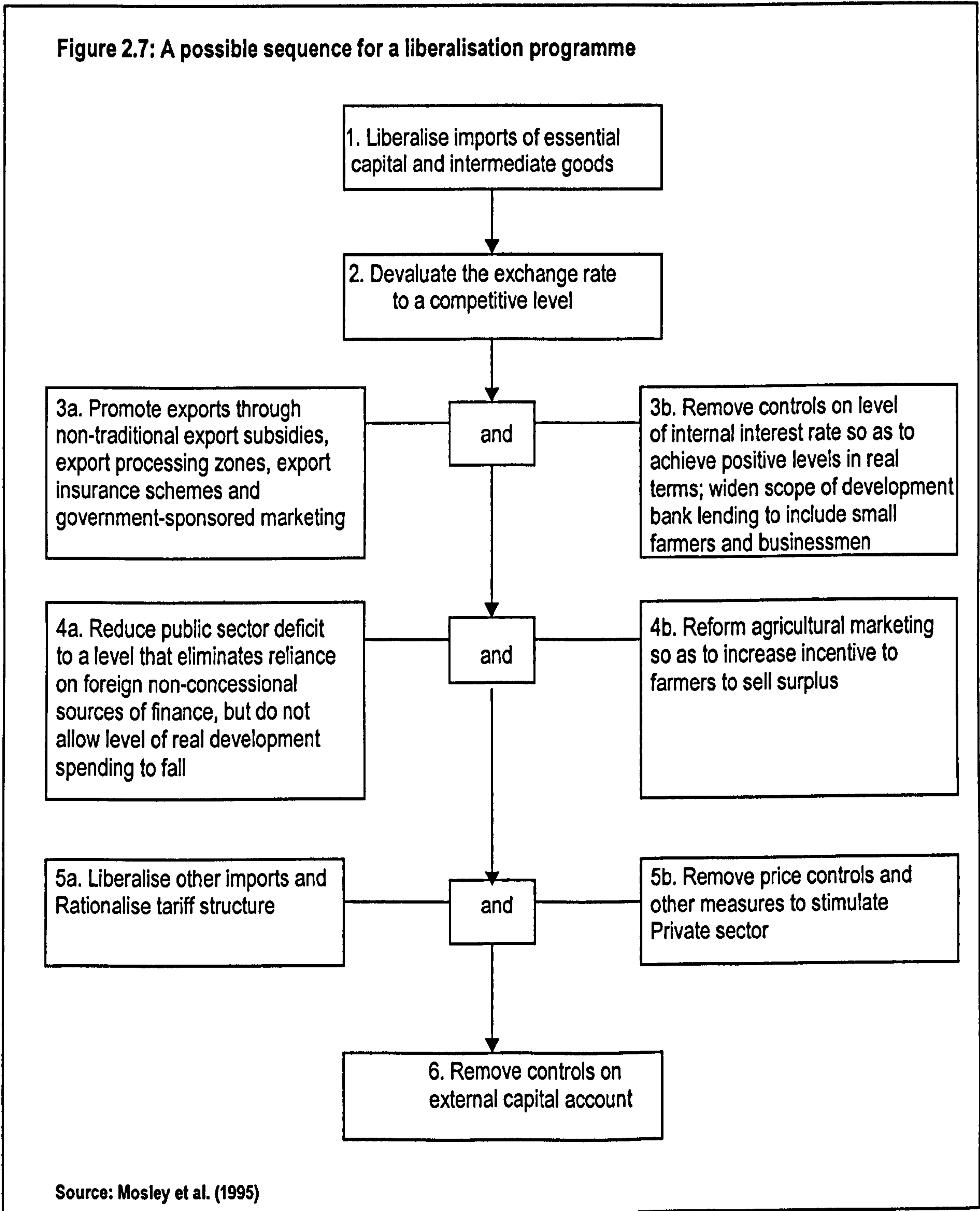
Expansion of SME markets beyond borders of SSA and participation in the global economy is required as part of the development process for the SMEs, and trade reform policies are meant to facilitate economic integration. However, it has been argued that the trade reforms, which Africa embarked on, have had modest gains in selected countries, and have met low acceptance and reversals in some (Mwaba 2003). Mwaba also argues that the reforms have not been adequate and that SSA needs to adopt deeper and significant policy and practical measures in order to increase their participation and integration in world markets. This would be a major step towards reversing the marginalisation of the continent and move towards the achievement of sustain long-term growth (Mwaba 2003). He further argued that while opening an economy to trade may not provide the desired quick fix, the removal or relaxation of quantitative import and export restrictions and lowering of tariffs would result in increased exports and growth and points out that trade liberalisation need not spell catastrophe for African economies as widely feared. (Mwaba 2003).

On another angle, Edwards (1984) argued that appropriate sequencing of structural adjustment reform is considered essential for the programme to have successful outcomes. Going back to the first two stages of the SAP described by Green (section 2.3.1), since the 1980s, countries have been implementing economic stabilisation policies followed by structural reform measures, such as trade liberalisation, privatisation, exchange rate devaluation, in no particular order and at different paces. It has been found that this approach has posed practical difficulties and inspired research efforts on the optimal sequence of the reform measures (Edwards 1986a, Corbo et al. 1987, Smith and Spooner 1989). Mosley et al. (1995) interpolated suggestions on the sequencing of the specific SAP measures and came up with a possible sketch of sequence, presented in Figure 2.7.

Different countries were recommended to follow different SAP reform sequence, depending on country circumstances, by the World Bank, and countries did not necessarily implement the measures in the recommended order. For instant, Malawi was advised to implement the specific



measures in the order of: 2 + 4a, 4b, 5a but had only implemented 2 followed by 4b by 1990 (Mosley et al. 1995).



It seems the adjusting countries were just picking and choosing whatever order of the measures that they thought suited them at the time and at own pace. So here, already it can be seen that the implementation process itself was distorted and hence the impact and outcome would be different from what the policy was intended to achieve. For example, worsening of BoP and increase in indebtedness of countries like Cameroon and Senegal is partly explained by premature trade



liberalisation, undertaken before the necessary exchange rate adjustment was achieved (Deverajan and de Melo 1987). However, it should be noted that appropriate sequencing of the SAP measures would be country-specific. Thus, removal of non-tariff barriers should largely be confined to intermediate inputs and capital goods at first and trade liberalisation should be undertaken in a country-specific manner. Countries with strong industrial base, such as Kenya, across-the-board liberalisation of consumer imports can lead to unnecessary de-industrialisation (Riddell, 1993). It has also been pointed out by Husain and Faruquee (1994), that reform measures should be attempted simultaneously and consistently as there is a close relationship between import liberalisation, public enterprise reform, government finance and financial sector reform.

Nevertheless, the general consensus emerging from the literature is that structural adjustment has not produced the intended outcomes and even towards the end of the 1980s, the IMF itself begun to express concerns over the overall growth and poverty impact of its programme (World Bank 1989b). In the late 1980s, the United Nations International Children's Fund (UNICEF) advocated "Adjustment with a Human Face" as an alternative set of policies designed to protect the poor during adjustment (Cornia et al. 1991). Soon after, the IMF and WB acknowledged the need to take into consideration the social consequences of adjustment. In a joint study prepared for the IMF's development committee in 1989, the IMF and WB admitted that there was a decline in per capita incomes accompanied by worsening social indicators, particularly in SSA and Latin America. They said that some of the poor did benefit, but many vulnerable groups were hurt by measures associated with adjustment (IMF/WB 1989). The report also said that by the mid-1980s, it became clear that given the time and effort required to turn deeply troubled economies around, it would be morally, politically and economically unacceptable to wait for resumed growth alone to reduce poverty. In majority of cases SAPs proved to have very serious consequences. Opening up of economies did not have the desired effect, rather poverty levels increased and cost of living rose (Willis 2005). There is a consensus that although SAPs may not have caused poverty in a direct sense, they certainly did not lead to poverty reduction (McIlwaine 2002). The UNDP have described the 1990s as a decade of despair for many countries and that 54 countries were poorer in 2003 than they were in 1990 (UNDP 2003).

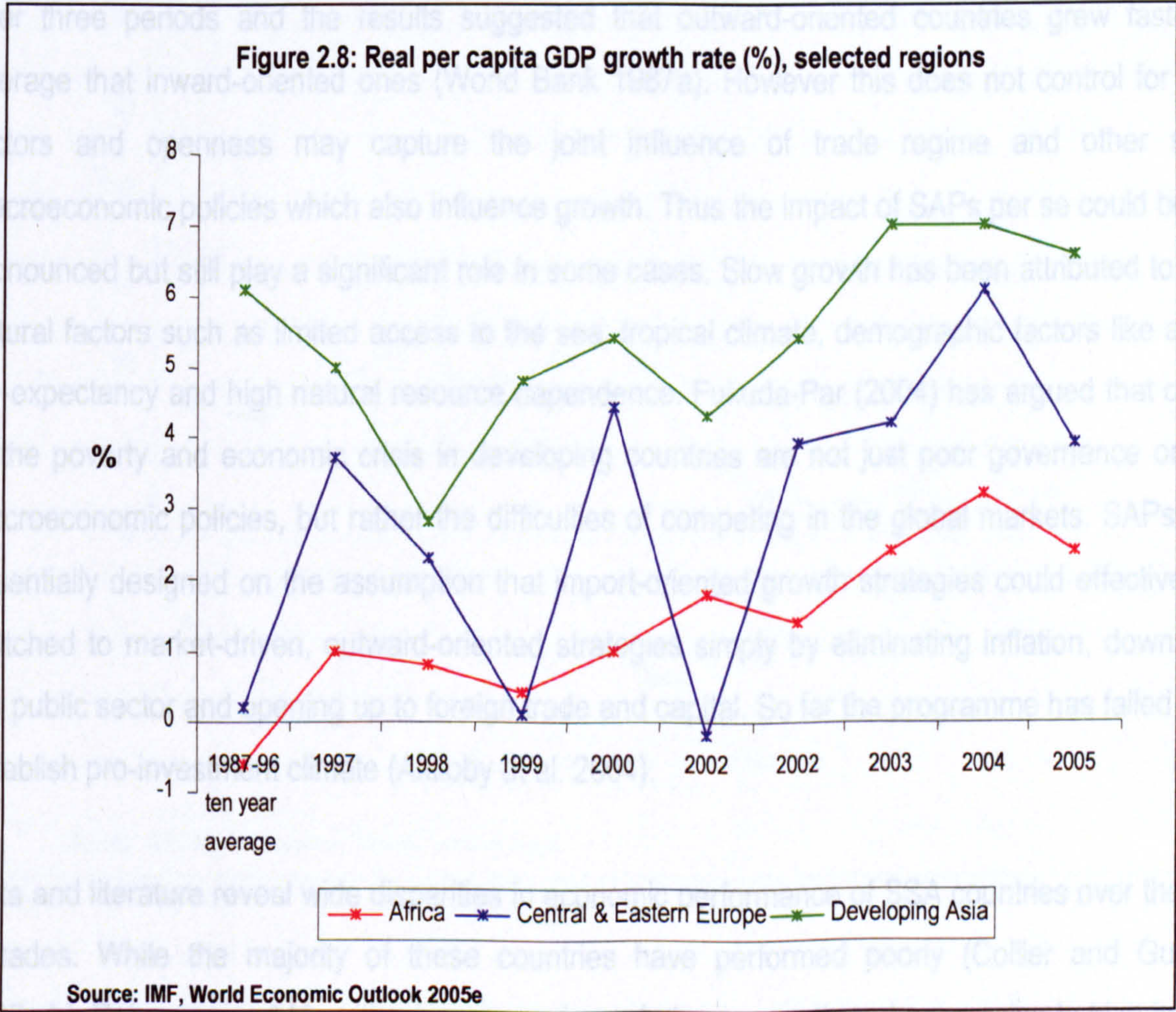
## **2.4 Economic Performance of SSA since independence**

Some analysts have viewed Africa's growth performance in relation to stages of political regimes and have argued that the economic performance of Africa has been affected by different policy choices made by the various political regimes (Ndulu and O'Connell 1999). During the post-



independence period, when most of these countries adopted single-party politics and authoritarian regimes, emphasis was on the importance of market-failure, inward-looking trade and investment policies and the need for state-led industrialisation. Ndulu and O'Connell pointed out that, although economic growth was adequate during that period, policy distortions and structural weaknesses in the public sector had already undermined the fiscal and BoP position when the shocks of the 1970s and early 1980s arrived. Inward policies failed to improve the living standards in Africa, and exacerbated the effects of the external shocks of the 1970s (Devarajan et al. 2001).

It has been argued that those countries that sustained appropriate market-based economic policies experienced positive economic growth during the 1970s and 1980s (Sachs and Warner 1995b). However, when compared to other developing regions, real per capita GDP has been poor for Africa as a whole, below 2% from the 1980s when the policy changes were first introduced for most countries up until 2003. Africa as a whole had the lowest per capita GDP growth rate of 2.4% in the world in 2005. Although there have been fluctuations and not fast enough per capita growth, overall the trend has been steadily moving in the upward direction (Figure 2.8).





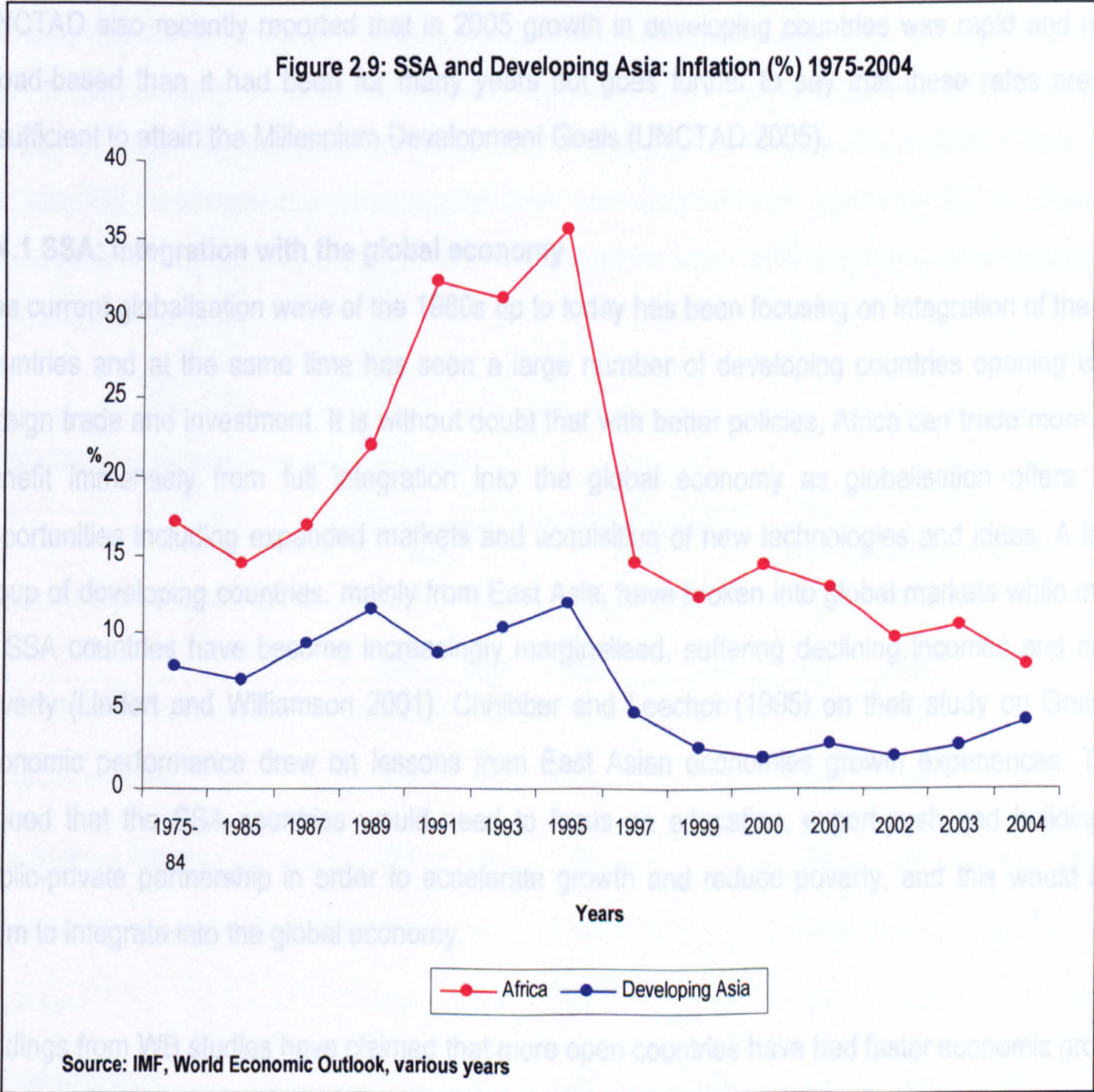
Ndulu and O'Connell (1999) argued that Africa's relative economic performance in the late 1980s, deteriorated further with the pressures and internal movements for democracy. The 1990s saw the transition from one-party rule to democracy for some SSA countries, and where the transition has taken place smoothly there has been a broad tendency towards rapid growth for several years after 1995. Successful reform is underpinned by a strong commitment to good governance and this is essential for rebuilding business confidence (Devarajan et al. 2001). Devarajan et al., in their analysis of ten African countries investigating how foreign aid affected economic policy in Africa, showed that successful reformers (Ghana and Uganda) had grown well in the 1990s and non-reformers such as Nigeria and Democratic Republic of Congo, had gone backwards rapidly. Devarajan et al. (2001) found that policy formation is primarily driven by domestic political economy although the study did not show any relationship between formal democratic institutions and good economic policy.

The World Bank classified the developing economies into four categories on the basis of trade orientation: strongly inward-oriented; moderately inward-oriented; moderate outward-oriented and; strongly outward-oriented. The trade orientation was then compared with average per capita growth over three periods and the results suggested that outward-oriented countries grew faster on average than inward-oriented ones (World Bank 1987a). However this does not control for other factors and openness may capture the joint influence of trade regime and other sound macroeconomic policies which also influence growth. Thus the impact of SAPs per se could be less pronounced but still play a significant role in some cases. Slow growth has been attributed to other natural factors such as limited access to the sea, tropical climate, demographic factors like as low life-expectancy and high natural resource dependence. Fukuda-Par (2004) has argued that origins of the poverty and economic crisis in developing countries are not just poor governance or poor macroeconomic policies, but rather the difficulties of competing in the global markets. SAPs were essentially designed on the assumption that import-oriented growth strategies could effectively be switched to market-driven, outward-oriented strategies simply by eliminating inflation, downsizing the public sector and opening up to foreign trade and capital. So far the programme has failed to re-establish pro-investment climate (Akitoby et al. 2004).

Data and literature reveal wide disparities in economic performance of SSA countries over the past decades. While the majority of these countries have performed poorly (Collier and Gunning 1999a,b), Botswana and Mauritius have experienced steady growth and converging to high income levels, thereby catching up with South Africa (Mehran et al. 1998). It is worth mentioning that



macroeconomic time series for developing countries are generally sparse and, when available, they are typically annual. Ideally to test the effect of growth, one would like to have both a long time series as well as a reasonably uniform cross-section of data. Nevertheless, the general picture, exhibited rising inflation, low (and often negative) GDP growth and stagnating investment rates in the 1990s (World Bank 1998a). Africa's inflation more than doubled from 8.5% in 1967 to 1975 period (IMF 1991) to 17% in the 1975 to 1984 period and increased to over 30% in the period between 1991 and 1995. The inflation did not fall back to below 10% until after 2003 when it came down to 7.8%, and recently the gap seems to be narrowing between Africa and developing Asia (Figure 2.9).



The economic performance in SSA is affected by high rates of inflation and inflation is a constraint on growth because it increases uncertainty about macroeconomic environment, which disrupts investment and savings decisions. A classical view is that high uncertainty due to bad



macroeconomic policy reduces the efficiency of price mechanism and this disrupts economic decision-making and slows down productivity growth (Pindyck and Solimano 1993). Fischer (1993) suggests that uncertainty reduces domestic investment and growth by inducing capital flight.

Despite underperformance of the 1990s and early 2000s, recent indications are that economically things are looking up for SSA. It has recently been reported that African economies registered their highest overall growth in eight years, of more than 5%, in 2004 (AfDB/OECD 2004). This was attributed to rising global commodity prices, expansion of its oil production, propitious weather conditions and steadily prudent economic policies. Another OECD/ADB joint report says that Africa is currently experiencing its best economic performance in many years and that solid growth is expected to continue in 2006, although at a slightly lower rate of 4.7% in 2005 (OECD/ADB 2005a). UNCTAD also recently reported that in 2005 growth in developing countries was rapid and more broad-based than it had been for many years but goes further to say that these rates are still insufficient to attain the Millennium Development Goals (UNCTAD 2005).

#### **2.4.1 SSA: Integration with the global economy**

The current globalisation wave of the 1980s up to today has been focusing on integration of the rich countries and at the same time has seen a large number of developing countries opening up to foreign trade and investment. It is without doubt that with better policies, Africa can trade more and benefit immensely from full integration into the global economy as globalisation offers new opportunities including expanded markets and acquisition of new technologies and ideas. A large group of developing countries, mainly from East Asia, have broken into global markets while many of SSA countries have become increasingly marginalised, suffering declining incomes and rising poverty (Lindert and Williamson 2001). Chhibber and Leechor (1995) on their study on Ghana's economic performance drew on lessons from East Asian economies growth experiences. They argued that the SSA countries would need to focus on education, export-push and building of public-private partnership in order to accelerate growth and reduce poverty, and this would help them to integrate into the global economy.

Findings from WB studies have claimed that more open countries have had faster economic growth and experienced no increase in inequality, thus integrating them more effectively into the world economy (World Bank 2002a). This is supported by Wade (2005) who argued that globalisation explains differences between countries, and that more open economies have a better record than less open ones or those who open slowly. However, evidence elsewhere showed that it was only



those countries which have been able to develop the export of manufactures which have fared better in the open economy (Oxfam 2002). It has been argued that effective integration into the world economy is not just a matter of opening up as evidenced by the fact that most SSA who opened up from the 1980s are still experiencing marginalisation rather than integration (Oxfam 2002). UNCTAD attributed this to the fact that these countries still rely on primary commodities, which are continuously suffering due to significant decline in market prices of the products, and failure to shift production into technology-intensive products (UNCTAD 2002b).

Trade remains the main vehicle for Africa's participation in the global economy and international trade is the first avenue by which most countries feel the impact of economic integration. One indication of increasing global economic integration is the growing importance of trade in the world economy and the importance of private capital flows to developing countries that have liberalised their financial markets. Merchandise trade is an important part of global trade and recent indications are that SSA merchandise trade increased from 42% of GDP in 1990 to 55% in 2004 (Table 2.5). And also FDI investment and private capital flows went up from those figures of 1990 in 2004 and this could be due to the fact that more and more countries have been opening up their economies as years have gone by.

**Table 2.5: Integration with the global economy**

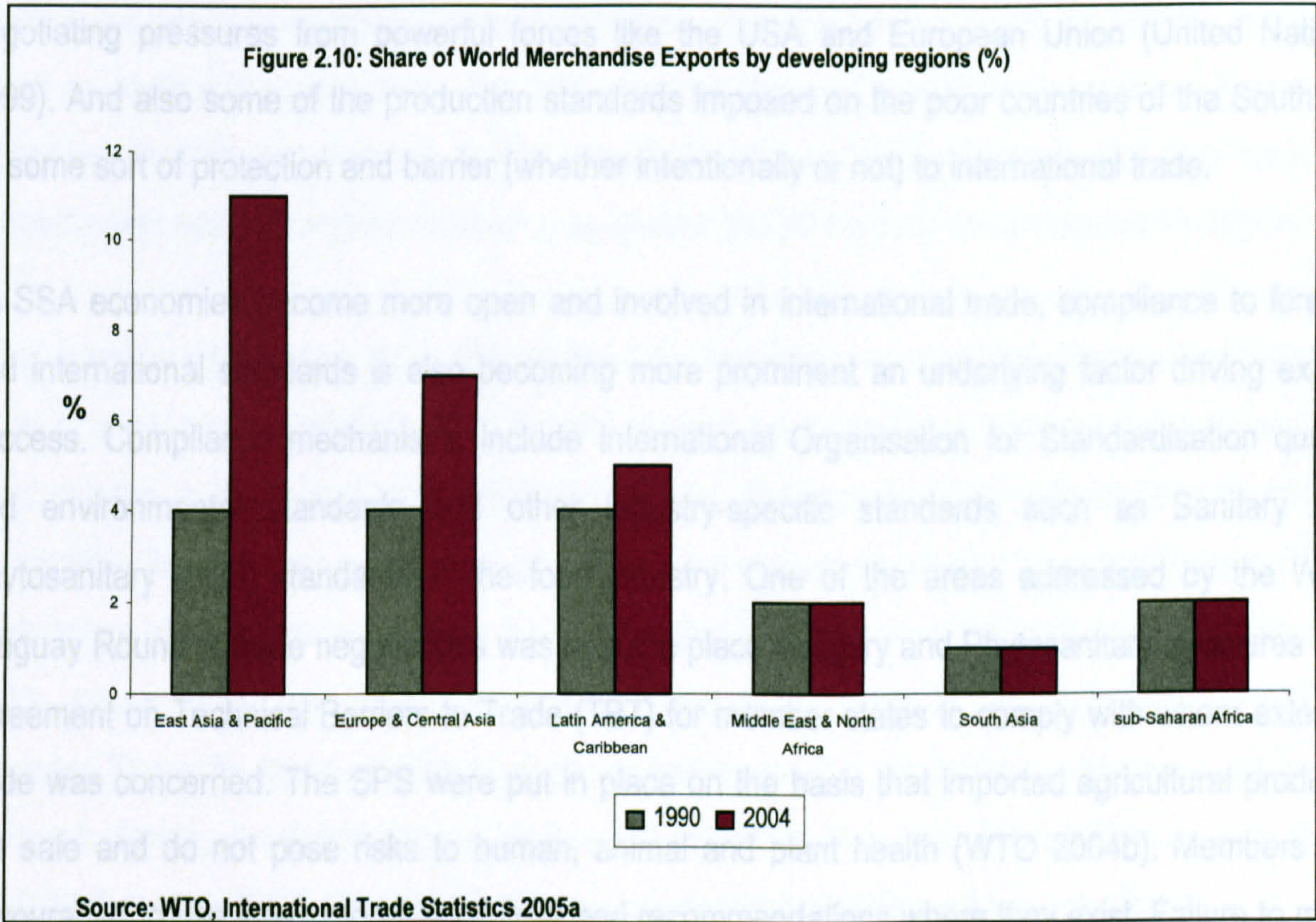
	Merchandise Trade (% of GDP)		Gross private Capital flows (% of GDP)		FDI Investment (% of GDP)			
	1990	2004	1990	2004	Net Inflows		Net Outflows	
	1990	2004	1990	2004	1990	2004	1990	2004
East Asia & Pacific	47.0	71.1	5.0	9.4	1.6	2.5	0.2	0.1
Europe & Central Asia	49.7	70.9	5.3	18.8	0.3	3.5	0.0	0.9
Latin America & Caribbean	23.3	44.6	8.0	10.4	0.8	3.0	0.1	0.7
Middle East & North Africa	42.9	55.1	4.9	..	0.3	1.1	0.0	..
South Asia	16.5	27.9	1.4	5.4	0.1	0.8	0.0	0.2
sub-Saharan Africa	42.4	54.7	5.1	9.5	0.4	2.2	0.0	0.3

Source: World Bank, World Development Indicators 2006b

.. = data not available



However, these are not sufficient indications of SSA integration into the global economy because other indicators tell a different story. For instance Figure 2.8 shows a decline in per capita GDP growth for Africa in the period 2004 and 2005, and there has been a rise in numbers of people living in extreme poverty in SSA. SSA's share of merchandise exports which stood at 2% in 1990 remained the same in 2004 (Figure 2.10). Overall developing countries' share of world exports increased by 11% from 1990 to 2004 and East Asia & Pacific was the biggest gainer capturing an additional 7%. For Africa, a share of less than 3% in world exports and less than 3% of FDI investment, even with the opening up of economies, shows how little integrated it is into the global economy.



As noted, the industrial sector in most SSA countries is largely based on the processing of primary products whose prices have been in decline. Other countries in the developed world do not suffer same problems as those of SSA on competitiveness because they are 'innovation-driven', competing in a wide range of industries producing unique products. Production and export of manufacturers is not well developed in most SSA. Although reliance on primary products in previous years worked well for SSA in terms of growth, the economic environment is different now as factor endowments have changed. Population growth and degradation of natural resources are amongst those factors that will dictate position of SSA in the export markets. The principle at work is that, in the absence of trade restrictions, the countries that can benefit most from trade are those



with good factor endowments, and geographical circumstances also need to be acknowledged in the light of trade liberalisation. Agricultural-based development cannot be entirely relied upon as semi-arid and vagrant weather conditions do pose problems for primary production.

Furthermore SSA has been experiencing protectionism of markets of the developed countries despite changing macroeconomic policies and opening up their economies so they could increase their share in international trade. There are serious issues associated with market access, export subsidies, resulting from protectionism behaviour of developed countries (Michalopoulos 1999). Globalisation as it relates to trade is aimed at reducing or eliminating protectionism in order to maintain a level-playing field of all trading nations. But if you are small and poor, you are subject to negotiating pressures from powerful forces like the USA and European Union (United Nations 1999). And also some of the production standards imposed on the poor countries of the South act as some sort of protection and barrier (whether intentionally or not) to international trade.

As SSA economies become more open and involved in international trade, compliance to foreign and international standards is also becoming more prominent an underlying factor driving export success. Compliance mechanisms include International Organisation for Standardisation quality and environmental standards and other industry-specific standards such as Sanitary and Phytosanitary (SPS) standards in the food industry. One of the areas addressed by the WTO Uruguay Round of trade negotiations was to put in place Sanitary and Phytosanitary measures and agreement on Technical Barriers to Trade (TBT) for member states to comply with where external trade was concerned. The SPS were put in place on the basis that imported agricultural products are safe and do not pose risks to human, animal and plant health (WTO 2004b). Members are encouraged to use international guidelines and recommendations where they exist. Failure to meet international standards for goods and to comply with the WTO SPS agreement can inhibit market access to export markets. Non-compliance affects the performance of the developing economies like Malawi because they have an impact on agriculture, which is the backbone of the economy. These measures could be seen by less developed member states as disguised barriers and restrictions on international trade and used to shield their own domestic producers from economic competition. On the other hand, the measures could be strategically used to enhance the competitive position of countries or individual enterprises, if resources permit.

However, developing countries face important challenges in the implementation of SPS and TBT agreements due to technical difficulties and resource constraints. Concerns were raised at the



Doha Ministerial Conference in 2001 regarding the implementation of various WTO agreements, including the SPS measures (WTO 2001a). Even if developed countries were to grant developing countries complete free access to their markets, supply-side constraints, such as standard compliance, would hinder them from enjoying significant gains from the full access. Non-tariff barriers such as 'Standards' are on the rise and this is a challenge for developing countries, especially exporters of mainly agricultural products and those venturing into exporting more process products as they lack trained manpower and equipment to address these non-tariff barriers and to comply with EU/WTO commitments and requirements. As an example, the EU requires that plants like tobacco be subjected to Phytosanitary tests and certified before they can be exported to the EU region (<http://www.export-help.cec.eu.int/>). This has cost implications for the exporting country as it needs to establish a natural plant protection organisation to inspect growing crops and report on pests and control them. The SSA countries may not be sufficiently equipped in terms of manpower to carry out rigorous analytical work to analyse WTO proposals and also there are concerns over cost of compliance which may impose budget burdens on development budgets.

A big question still remains as to why much of the developing economies still remain excluded, in terms of economic convergence, from the globalisation episodes. Some have argued that even with good policies, a landlocked malaria-infested country, like Malawi simply will not be economically competitive. As well as opening trade, geography also matters for growth. Transport costs to OECD markets are higher than the tariff on their goods due to adverse geography (Lima and Venables 2000). Ades and Glaser (1999) focus on openness in the sense of access to seaports and rail services. There is literature stressing geographical position as a factor governing long-term economic development and why Africa has not benefited from globalisation (Bloom and Sachs 1998, Gallup et al. 1998). Tropical location and demographic burden are amongst them.

The tropics, especially Africa, is said to have lower agricultural productivity compared to the mid-latitudes where most of humanity resides. A lot of SSA is extremely vulnerable to drought, has the highest variance around annual average rainfall, and a lot of coastal East Africa is hot and arid. More to the point, transportation is most difficult in Africa: only 19% of Africa's population live within 100km of the coast. Furthermore, there is also special disease burden in tropical Africa, involving infectious and parasitic diseases such as malaria. It has been argued that the poor geographical and demographic endowments in Africa in turn cause policy failure and hinder good governance (Bloom and Sachs 1998, Davis 2001, Gallup et al. 1998). Collier and Gunning concluded that since the 1980s integration of markets has enabled only those developing countries with reasonable



locations, policies, institutions and infrastructure to harness their abundant labour to give themselves a competitive advantage in some manufacturers and services (Collier and Gunning, 1999b). However, a United Nations Development Programme (UNDP) report has argued that geography should not be an impediment as it can be overcome by better roads, communication and deeper integration with neighbouring countries (UNDP 2003).

Information, Communication and Technology (ICT) also plays an important role in today's economic integration. However, not all countries' Information, Communication and Technology infrastructure is well developed and this could be one reason why some less developed countries in SSA are being marginalised as they cannot keep up with new technologies and market information and are remotely placed geographically. In an increasingly global-knowledge-based economy, information and communication technologies can be vital tools in helping SSA countries to become more competitive, both regionally and globally. SSA can harness ICT to move up the value chain and compete more efficiently so as to promote broader economic growth. Table 2.6 presents selected data on information and technology access in selected SSA countries for 2003. As Malawi is the focus of this study, Malawi's ICT data is highlighted.

From the table it can be seen that there is a variation in the length of time it takes for a business to just obtain a telephone line. For instance, in Malawi it takes an average of 75 days compared to South Africa where it takes about a week. Malawi firms suffer the longest period (55 hours) in duration of telephone outages and this obviously has impact on business operations and contact with customers and suppliers. Malawi has only one telephone operator, a second one licensed in 2003, was not yet operational in 2005, and there are only two mobile phone operators with a total of 260,000 subscribers. As for the internet, there are 19 licensed internet providers of which 8 were operational in 2003 with an estimated 13,000 subscribers and an estimated 50,000 to 75,000 users in total (UNDP 2005a). All dial-up connections to the internet are treated as local calls which may be a discouragement for profit-driven internet service providers but affordable for some individuals in the country. With low numbers of telephone, mobile phone and internet users, application of ICT to enable development can hardly be achieved and business would definitely struggle to compete globally and interact with international suppliers and potential customers.

Table 2.6 also reveals that not many firms in Malawi and SSA in general use the World Wide Web to interact with customers and suppliers. In fact it is less than 35% of the firms in most of the countries presented here. However Malawi has a higher interaction through email (67%) than Benin



(36%), Mali (42%), Tanzania (58%) and Uganda (39%). Furthermore, the distribution of ICT and related infrastructure is uneven and in favour of urban settlement in Malawi.

**Table 2.6: Information and Technology indicators in selected SSA countries, 2003**

	Malawi	Zambia	Benin	Kenya	South Africa	Mali	Tanzania	Uganda
Delays in obtaining main telephone line connection (days)	74.61	54.79	130.97	80.59	6.58	50.95	18.32	25.38
Telephone access: fixed mainlines (per 1000 people)	7	8	9	9	103	6	4	3
Mobile phone subscribers (per 1000 people)	18	26	30	76	413	30	44	42
Faults (per 1000 mainlines)	59.60	124.90	6.20	149.10	48.20	177.60	24.00	16.60
Unavailable telephone services (days)	10.26	23.55	16.60	28.75	4.40	8.76	37.42	10.49
Duration of telephone outages (hrs)	55.29	11.04	6.07	20.20	3.35	10.26	9.20	14.79
Daily newspapers (per 1000 people)	2	22	5	8	25	1	..	3
Households with television set (%)	2	26	20	19	54	15	14	6
Access to personal computers (per 1000 people)	2	10	4	13	82	3	7	4
Internet users (per 1000 people)	4	20	12	45	78	4	9	7
Firms using Web interaction with clients/suppliers (%)	23.27	27.18	24.87	32.00	70.81	28.57	23.48	10.00
Firms using email to interact with clients/suppliers (%)	67.30	83.50	35.53	78.42	98.34	41.83	58.43	38.67
Firms using new production technology (%)	37.97	49.76	..	..	60.57	49.57	31.97	47.33

Source: World Bank, Enterprise Survey Query Online Database, 2003c

.. = data not available

Communication networks and related services are concentrated in the major urban centres and this excludes over 85% of the population that lives in rural areas. With most people being poor and residing in the rural areas where electrical power is also limited, community radio network has the highest potential of reaching these communities. There are 15 radio stations and one main television station with other subscription-based commercial satellite and cable television services in Malawi, largely available to the urban population. Circulation of newspapers is also concentrated in



the capital city and main urban centres and never reaches the rural communities with poverty and remoteness being the principal barriers to access to most of these forms of communication. Clearly with underdeveloped information media, the Malawi SMEs (which are mostly rural-based) have very little chance of receiving up-to-date information on new production technologies and markets outside their local areas let alone international markets. As can be seen from Table 2.6, only 38% of the Malawi firms were using new production technology in 2003. Malawi has limited access to ICT infrastructure and services and the high costs of those services, particularly international calls and high-speed internet access, which are crucial to firm competitiveness in this information and technology age, are underdeveloped.

As for communication in terms of transport networks, Malawi is said to have a good road network and railway services which connect imports and exports to important ports of Beira and Nacala in Mozambique and port of Durban in South Africa. However it has been reported that the roads themselves are in bad physical shape and road maintenance is not up to standards. (AfDB/OECD 2006). For those parts of the country where the roads are in poor condition it means that domestic transport cost is much higher and hence the benefits of a more liberalised market have not yet reached their producers and consumers. High transport costs are recognised as one of the major factors that make Malawi's goods uncompetitive in domestic and international markets.

Malawi is 860Km to the nearest seaport, Nacala in Mozambique, from the Capital, Lilongwe and there is only 717 Km operational single track public railway line extending from near the Mozambique border in the South of the country through to Salima in the Central and then goes West through Lilongwe to Mchinji and the Zambian border. Most of Malawi's foreign trade is conducted via Salima, a port on Lake Malawi, which is connected by rail with the seaport of Nacala. The rail transport is mainly used to carry freight, and it used to be the main mode of transport for Malawi's foreign trade before the lines to Beira and Nacala ports in Mozambique were severely damaged in the 1984/85 civil war in Mozambique. When the transport communication through the transit country of Mozambique experienced disruption by the civil war, Malawi was cut off economically and this affected the international trade flow.

As for air transport, there are a total of 43 airport runways of which only 6 are paved and again this is a constraint to businesses for a landlocked country which needs all modes of transport communications it can get in order to link up with the rest of the world and to be competitive. Furthermore, airfreight services have been cut and there is more usage of regional hub airports for



international flight links. There are no direct links between Malawi and Europe, which also contributes to the high cost of air freight services out of Malawi (AfDB/OECD 2006). Most SMEs in Malawi mainly depend on the road network. Unfortunately the transport infrastructure is concentrated in major cities, towns and urban centres and along the main connecting roads which means that many SMEs are in remote areas and hence impact on their performance. Transport is a very significant factor to the Malawi economy. For example in the case of agricultural export commodities, most entrepreneurs will just resort to subsistence agriculture and domestic production as they cannot absorb international transport costs. Cost of shipping goods is too high for SMEs and interest charges on inventories and goods in transit cause disruption of domestic production due to non-arrival of inputs and loss of orders due to inability to effect reliable delivery of goods to markets. This results in worsening terms of trade, reduced export competitiveness and export range and volumes.

From the data presented in Table 2.6, it can be said that Malawi, like most other SSA countries, is not well integrated into the global economy in terms of ICT partly due to its landlocked nature and partly due to being one of the poorest countries in the world and hence cannot afford to maintain its road infrastructure to properly connect rural populations to other parts of the country and to afford new advanced forms of communication such as the internet and email, and television media. The integration process within SSA countries themselves is essential towards achieving international competitiveness for their economic growth.

Although trade has been opened up, for those landlocked countries like Malawi, there still exists the issue of natural protection of high transport costs. Landlocked countries suffer from 'remoteness' which causes greater delays and poor communication with overseas markets and input suppliers, and affects development potential for export. The landlocked countries have to depend on transit coastal countries and this raises transportation costs, as the case for Malawi, and consequently increases the price of imported goods and lowers the price received domestically for exports, thus competitiveness is related to distance. Furthermore, the reality is that some investors may see no reason why they should locate in a land-locked country when there is a neighbouring transit coastal country where labour is as cheap and they would not incur high transport costs. So it can be said that even with trade liberalisation, the land-locked nature of the poor countries, compounded by reliance on production of primary commodities, pose problems for both local producers and external investors.



It has also been argued elsewhere that opening up to international trade has led to an increase in the gap between the national income of the poor and rich nations (Ravenhill 1993). Economy is much more complex than just advocating free markets, free trade and minimal government intervention and this does not necessarily lead to economic growth or development. A study by the UNDP on the relationship between trade liberalisation and high growth rates in India and China showed that trade liberalisation followed rather than preceded high growth in these countries (UNDP 2002). Thomas (2005: p336) argued that these findings suggest that, "the free trade mantra which still dominates IMF/WB/WTO policy on how to promote global economic integration (and therefore development) may well be misplaced". She argues further that states need to be mindful in their application of trade liberalisation, and not see it as an end in itself which will necessarily bring the desired results.

The most important effect of globalisation is that it increases competition and 'those who realign their practices most effectively to Information Age Standards can reap the most benefits' (IDC 2001:35 and UNIDO 2001c). However, many developing countries do not have the necessary and sufficient resources, capacities and competencies to manage globalisation in order to maximise its potential benefits and minimise its inevitable unintended adverse consequences. Kiggundu (2002b) suggested that these economies need to establish public-private partnerships, both domestically and internationally, in order to manage the various dimensions of globalisation. The international community, businesses, institutions and governments have a role to play to facilitate effective globalisation in the rest of the world.

#### **2.4.2 SSA and Regional Integration**

In recent years many SSA countries have taken the stance that regional groupings will help them integrate more into the global economy and as such free-trade groupings have been growing in numbers. Thus, in order to boost trade among African countries, regional economic communities have been created over the last few decades. These include, Economic Community of West African States (ECOWAS), Central African Monetary and Economic Community (CEMAC), the Economic Community for Central African States (ECCAS), East African Community (EAC), Southern African Customs Union (SACU), Southern African Development Community (SADC), Common Market for Eastern and Southern Africa (COMESA). The importance of economic co-operation for Africa derives mainly from the opportunities that emanate from integrating the markets of individual countries in the continent. Smallness in size, of most of the countries, has been described as a major obstacle to Africa's economic development (ADB 2000). The rationale is that, with regional free-trade groupings, the export market will widen the total market for a country's producers like



SMEs. It is believed that collaborative efforts across spatial territorial boundaries in Africa would allow for aggregate economic benefits and overall development (Adedeji 2002).

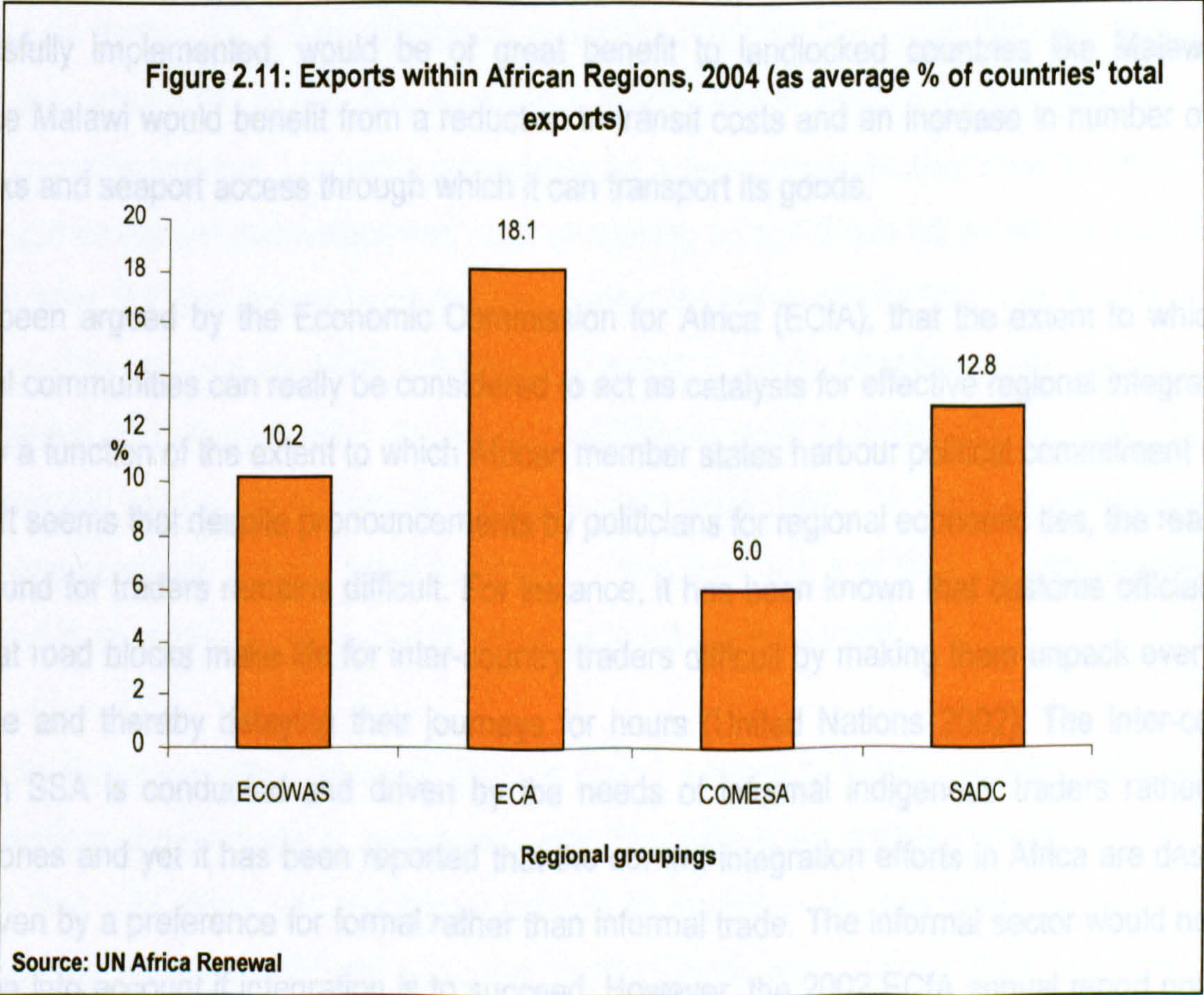
The regional groupings were meant to foster or act as building blocks for regional integration in Africa, but they seem to be failing to do so. Some of the factors, highlighted as reasons for the failure of the regional groupings in Africa include: lack of political will to establish effective intra-national institutions and to implement agreed treaties and protocols; overlapping memberships; and inadequate mechanisms for equitable sharing of costs and benefits of integration (Adedeji 2002). The problem is that there are so many regional cooperation bodies in Africa, some of which are overlapping and causing conflicting spheres of jurisdiction, where different organisations in the same region have the same mandate or where a country, like Malawi, belongs to two or more organisations that are pursuing different policies at a particular time (ARIA II 2006). Malawi is a member of both SADC and COMESA both whose agendas include promoting regional integration through trade development and ultimately declaring free trade areas in the future.

Indications are that most of these integrations have not met expectations and that much remains to be done to achieve the declared objectives. Overall, trade amongst African countries account for less than 20% of their total external trade, the lowest of any world region (ECfA 2002). And also the average percentage of SSA countries' total exports within each of the different economic groups is less than 20% (Figure 2.11). The regional groupings offer advantages of certainty and improved access, which is an attribute of multilateral negotiations, though for a limited range of commodities, considering that most of these countries produce similar types of goods and hence limiting the trade between each other. By producing and exporting similar raw materials, and not processed goods, there is very little that they would be interested in importing from one another. A World Bank study reported that intra-African trade is dominated by a handful of countries, selling a handful of products. Excluding South Africa, only five SSA countries, Cote d'Ivoire, Ghana, Kenya, Nigeria and Zimbabwe provide three-quarters of all intra-Africa's exports, and manufactured goods account for only 15% of such trade (World Bank 1998b).

In addition to producing similar products (and mainly raw materials), poor infrastructure, inefficient transport and communication system are a major cause of Africa's low competitiveness and low levels of inter-country trade. As discussed before, the infrastructure and communication networks are not that strong in Africa. The continent's railways and roads often lead towards the ports rather than link countries across regions. For instance, it has been argued that because of hindrances to



trade within Africa, exports from Tunisia and Cameroon often find their way to French warehouses before being redirected to each others markets' shelves (United Nations 2002). In order to allow trade to flow regionally, investment in physical infrastructure, railway, roads, power lines, air services and telecommunication would be necessary. Although there has been a formation of so many of the regional trade groupings, it does not necessarily mean that the transport costs would automatically reduce as there are other issues involved. Problems which have been identified in the regional transport and communication sector include: slow process of the creation of autonomous road agencies and boards to manage road funds and to ensure co-ordinated road development and maintenance; lack of regionally established policy framework under which governments and the private sector should deliver road infrastructure and related services; inadequate expenditure on rehabilitation of road infrastructure; road infrastructure in some countries being poor due to bombings (civil war) and neglect; some railways have become unsafe for the passage of trains; failure of national railway operators to provide a reliable, predictable and cost-efficient service; congestion in some seaports because of mismanagement; and inadequate security at the seaports hence poor safety leading to high insurance premiums (Vogelaar and van Dijk 2003). All these issues would have to be resolved before the member countries started to realise the benefits of integrating transport networks





For land-locked countries like Malawi, working together with other and coastal countries at regional level in order to lower the high cost of transport, is imperative. A greater regional integration would be a stepping stone to broader integration into the global economy. Regional cooperation is virtually important for SSA's economic development and future international trade. Through cooperation and integration, regional planning frameworks and trading blocks make more efficient use of collective capital, labour and natural resources of member states. The economies of scale in productive investments such as for large infrastructure and utilities projects reduce cost. Where the landlocked countries cooperate closely, they can benefit from an efficient-run, low-cost transport corridor. They would need to foster a transport corridor under which joint interests can most easily be pursued (Livingstone 2002).

In recent years there has been a renewed emphasis on building regional infrastructure as crucial to Africa's integrated development (ECfA 2004:36). SADC has currently measures in place to integrate transport infrastructure and services across its member states. And also work is underway to improve the quality of transport links that are in poor condition, along regional corridors, providing outlets to the sea for the landlocked member countries (SADC 2006). The COMESA is also in the process of implementing programmes to improve the transport and communication systems of the region and working towards harmonising road transit charges. All these initiatives should they be successfully implemented, would be of great benefit to landlocked countries like Malawi. For instance Malawi would benefit from a reduction in transit costs and an increase in number of road networks and seaport access through which it can transport its goods.

It has been argued by the Economic Commission for Africa (ECfA), that the extent to which the regional communities can really be considered to act as catalysts for effective regional integration is actually a function of the extent to which African member states harbour political commitment (ECfA 2002). It seems that despite pronouncements by politicians for regional economic ties, the reality on the ground for traders remains difficult. For instance, it has been known that customs officials and police at road blocks make life for inter-country traders difficult by making them unpack every little package and thereby delaying their journeys for hours (United Nations 2002). The inter-country trade in SSA is conducted and driven by the needs of informal indigenous traders rather than formal ones and yet it has been reported that the current integration efforts in Africa are designed and driven by a preference for formal rather than informal trade. The informal sector would need to be taken into account if integration is to succeed. However, the 2002 ECfA annual report points to



the East Africa Community as beginning to incorporate the informal sector into its activities (ECfA 2002).

Ultimately, the creation of regional markets in Africa would enhance industrial efficiency as larger markets allow exploitation of economies of scale. It has been argued that regional integration would offer best hope for SSA to integrate further with the rest of the world (ADB 2000). Wider regional markets would open up more opportunities for both producers and consumers, beyond the small markets (of some) within their borders. Mobility across borders and harmonised policies could spur faster economic growth and provide greater opportunities to attract investors. Although it may seem a long way yet for countries like Malawi to benefit from regional co-operation, it seems initiatives are in place and discussions are underway for solving some of the problems.

### **2.4.3 SSA: Opening up and FDI**

With the help of modern technology in transport and communication, businesses and financial flows move through the world allowing international trade and FDI to grow significantly over the last four decades. FDI is driven by broad-based economic policy reforms and it was expected that accelerating the pace of liberalisation, deregulation and privatisation would attract FDI to Africa (IMF 1999b, World Bank 1997c). Privatisation of state-owned enterprises has been, and is becoming an avenue for foreign investment and many countries have used this channel to attract FDI. Mkandawire (2001) argued that attracting FDI is the key to bringing the resource gap of low-income countries and that it provides the catalyst for a 'late industrialisation' drive to Africa. It was also argued elsewhere that accelerated pace of opening up to FDI will bring not only more stable capital inflows but also greater technological know-how, higher-paying jobs, entrepreneurial and workplace skills and new export opportunities (Prasad et al. 2003). Most developing countries have been opening up their economies to international trade in order to attract FDI and many of them have reformed trade policy in order to qualify as open economies. FDI plays an important role in accelerating economic growth. Table 2.7 shows a selected number of SSA countries classified by Sachs and Warner (1995a) according to openness to international trade.

Sachs and Warner described an economy to be open if average tariff rate was below 40%; average quota and licensing coverage of imports was less than 40%; black market exchange rate premium was less than 20%; there was no extreme controls on exports in terms of taxes, quotas, and state monopoly; and was not considered a socialist country (Sachs and Warner 1995a). According to the



'Sachs and Warner' criteria, not many of the SSA countries were regarded as open in 1990, and apart from Mauritius and Botswana they were all below 40% open.

<b>Table 2.7: Market-oriented pro-growth economic reform in Africa, selected countries</b>		
	<b>Openness to International trade</b>	<b>Year of Opening</b>
<b>Consensus Reformers:</b>		
Botswana	0.42	1979
Gambia	0.19	1986
Ghana	0.23	1991
Guinea-Bissau	0.17	1987
Mauritius	1.00	1968
Uganda	0.12	1988
<b>Partial Reformers:</b>		
Benin	0.04	1965-90
Cameroon	0.00	1965-90
Kenya	0.12	1965-90
Madagascar	0.00	1965-90
Malawi	0.00	1965-90
Mali	0.12	1965-90
Mauritania	0.00	1965-90
Nigeria	1.00	1965-90
South Africa	0.00	1965-90
Zambia	0.00	1965-90
<b>Source: Sachs and Warner (1995a)</b>		
<b>Note: 1 = a high degree of openness, 0 = low degree of openness</b>		

It can also be seen from the table that Malawi was one of the late reformers and had a zero degree of openness in 1990. Most of the countries have been carrying out the reforms inconsistently and partially. It has been argued that timeliness, sustainability and consistency are crucial for investor confidence. Thus inappropriate design and implementation of adjustment policies may prolong or contribute to macroeconomic instability and uncertainty and thus affect FDI (Offerdal 1996). It has been argued that those poor countries that have followed standard market-based economic policies, including opening to international trade, have experienced more integration and economic growth (Sachs and Warner 1995b).

However, despite SSA countries opening up their economies and complying with policy advice of accelerating the pace of liberalisation, deregulation and privatisation, the record of the past decades with respect to reducing poverty and attracting FDI to SSA has been disappointing and it has been suggested that the exclusive emphasis on market-oriented reform and governance as determinants of the size of FDI flows to Africa is misleading (UNCTAD 2005). Although about 35%



of global FDI went to developing countries in 2004, the SSA region received less than 2% of it , half of what it was in the 1970s (Table 2.8).

**Table 2.8: Share of FDI inflows to developing regions (%), 1970-2004**

	1970-1979	1980-1989	1990-1999	2000	2001	2002	2003	2004
Developing Countries	25.3	22.7	30.4	18.2	26.9	23.2	30.7	35.9
Africa	4.4	2.3	1.5	0.6	2.4	1.7	2.7	2.8
North Africa	0.7	0.9	0.5	0.2	0.6	0.4	0.8	0.8
sub-Saharan Africa	3.8	1.4	1.1	0.4	1.8	1.3	1.9	1.9
Latin America & the Caribbean	13.6	7.9	11.1	7.0	10.8	7.6	8.9	10.4
Asia & the Pacific	7.4	12.5	17.7	10.5	13.7	13.9	19.2	22.8

**Source: UNCTAD, Handbook of Statistics, various years**

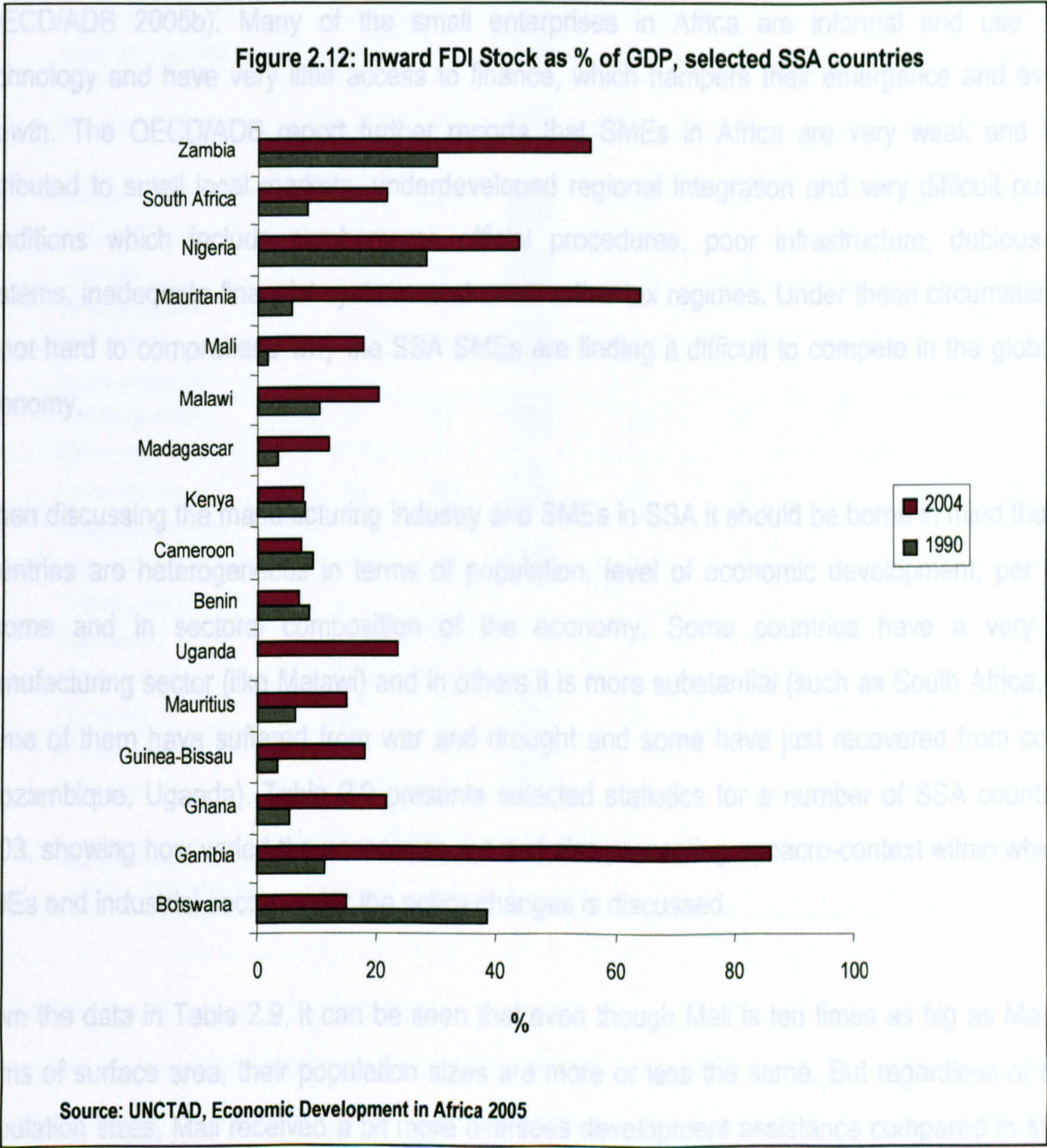
Simply adoption of open trade does not guarantee integration of the developing counties into the global economy as evidenced by many poor countries which have opened up their economies since the 1980s but have fallen behind in terms of both income levels and structural developments (Dowrick and DeLong 2001). It has been argued that the outcome of increased integration into the world economy need not be due to changes in trade policy only but also reliable property rights, strong rule of law and macroeconomic stability are also associated with more trade and FDI (Dollar and Zoldo-Lobaton 2001).

Other factors such as market size and growth, resource endowments and infrastructural developments are also significant determinants of the pattern of FDI flows to Africa. Limao and Venables (2000) have even argued, on the extreme, that for some countries, continued marginalisation is a reality. They argue that due to disadvantages of location they probably have little realistic prospects of developing. Attracting FDI through greater openness and downsizing of the states has not been empirically proven. As can be seen from Figure 2.12, countries like Zambia and Nigeria had much more FDI stock inflow as a percentage of GDP in 1990 than Mauritius and Uganda which were categorised as more open economies during that time.

It has been reported by UNCTAD that extraction of Africa's natural resources accounts for the uneven spread of FDI flows across the continent. Those countries classified by the World Bank as oil- and mineral-dependent have, on average, accounted for close to three-quarters of annual FDI flows over the past two decades (UNCTAD 2005). This would explain why countries like Zambia,



Nigeria and Botswana showed higher percentages of FDI inflow stock as these countries have copper, oil and diamond mines respectively. As a result of reforms, Africa has become much more 'attractive' as a location for mining FDI. For example, Mali which had one of the lowest percentages of FDI stock inflow in 1990, did not have a large-scale mining sector before the 1990s, but has recently been reported to host considerable flows of FDI as has Tanzania (Campbell 2004).



The singular focus on attracting FDI through greater openness seems to have drawn attention away from more fundamental determinants of FDI flows to Africa – namely market size and growth, resource endowments and infrastructural development. Particular combinations of geographical, historical and structural features have traditionally attracted FDI into enclaves of export-oriented primary production with limited linkages to the rest of the economy. Lall (2004) pointed out that



investment in skills, technology and infrastructure is needed if countries are to successfully attract FDI and integrate more effectively into the wider development strategies.

## **2.5 SSA: SMEs, Manufacturing and Industry performance under the policy changes**

The manufacturing sector in African economies has been described to consist mostly of small companies alongside large firms with not very many medium-sized modern factory firms in between (OECD/ADB 2005b). Many of the small enterprises in Africa are informal and use simple technology and have very little access to finance, which hampers their emergence and eventual growth. The OECD/ADB report further reports that SMEs in Africa are very weak and this is attributed to small local markets, underdeveloped regional integration and very difficult business conditions which include cumbersome official procedures, poor infrastructure, dubious legal systems, inadequate financial systems and unattractive tax regimes. Under these circumstances it is not hard to comprehend why the SSA SMEs are finding it difficult to compete in the globalising economy.

When discussing the manufacturing industry and SMEs in SSA it should be borne in mind that SSA countries are heterogeneous in terms of population, level of economic development, per capita income and in sectoral composition of the economy. Some countries have a very small manufacturing sector (like Malawi) and in others it is more substantial (such as South Africa, Mali). Some of them have suffered from war and drought and some have just recovered from conflicts (Mozambique, Uganda). Table 2.9 presents selected statistics for a number of SSA countries in 2003, showing how varied the economies are and also presenting a macro-context within which the SMEs and industrial sector under the policy changes is discussed.

From the data in Table 2.9, it can be seen that even though Mali is ten times as big as Malawi in terms of surface area, their population sizes are more or less the same. But regardless of similar population sizes, Mali received a bit more overseas development assistance compared to Malawi, in 2003. Also, in comparison to the other selected SSA countries, Malawi had the lowest GDP per capita and the lowest FDI net inflows in 2003. However, Malawi had the highest merchandise trade as a percentage of GDP (66%) compared to the other countries, although performance of manufactured exports was relatively poor (12%).



**Table 2.9: Selected statistics for selected SSA countries, 2003**

	Benin	Kenya	Malawi	South Africa	Mali	Tanzania	Uganda	Zambia
Surface area (sq. km)	112,620	580,370	118,480	1,219,090	1,240,190	945,090	241,040	752,610
Population, total (to the nearest million)	8	33	12	46	12	37	27	11
Official Development Assistance US\$ (mill)	293	514	518	625	543	1,704	976	581
Real GDP growth (%)	4	1.7	4.4	2.8	7	6.3	7.1	4.3
GDP per capita (US\$)	517	1,037	156	3,489	371	287	249	417
Inflation, GDP deflator (annual %)	6	7	9	4	1	6	10	20
Merchandise trade (% of GDP)	37	41	66	47	47	33	29	58
Exports of goods & services (% of GDP)	14	24	27	28	27	18	12	21
Primary exports (% of merchandise exports)	92	76	88	58	60	82	91	86
Manufactured exports (% of merchandise exports)	8	24	12	42	40	18	9	14
Total debt service (% of exports)	8	16	..	9	6	5	7	..
Industry Value Added (% of GDP)	14	17	16	32	26	16	21	27
FDI, net inflows US\$ million	48	82	10	770	132	254	202	172
<b>Source: World Bank, WDI 2003</b> .. = data not available								

### 2.5.1 SSA: the Manufacturing industry

For most of the SSA countries the private sector is predominantly agricultural rather than manufacturing. It is said that Africa has a comparative disadvantage in manufacturing and that manufacturing industry in these countries has always been focusing on relatively low-technology industrial activities from the beginning, whereas some writers have argued that SSA has been experiencing de-industrialisation (a decline in manufacturing) in recent decades. It should be noted here that in the literature there seem to be different definitions and interpretation of 'de-industrialisation' (Jalilian and Weiss 2000, World Bank 1994), resulting in different interpretation of statistical evidence regarding whether SSA's de-industrialisation is the effect or reason of SAP and trade liberalisation, hence a diversity in views (Jalilian et al. 2000).



On one side, it has been argued that SAPs have had harmful effects on SSA industry, wiping out important parts of industrial base for future growth (Lall 1992, Stein 1992). Stein (1992) argued that the WB/IMF policies were likely to de-industrialise countries and force them to rely on resource and agricultural exports. Bennell (1998) also argued that all those industrial enterprises which were heavily protected through import-substitution policies, would not be able to survive under open economy conditions as some of them stood very little chance of becoming internationally competitive. Indicators from an analysis by Noorbakhsh and Alberto (2000) show that, in general, there was very little progress made since 1980-85 and that there has been a worsening of the situation in 1991-94. They argue that the gap between SSA and other countries has been widening over time, leading to marginalisation of industry in Africa, even where SSA is improving.

On the other side, it has been argued that SSA was not even 'industrialised' before the SAPs hence no particular regional problems. In their study, Jalilian and Weiss (2000) found little evidence for any support for the de-industrialisation's problem in SSA that was more than what was happening everywhere else. They argue that what is being observed could be the shrinking of inefficient, previously protected, activities and reallocation of resources in a direction in line with comparative advantage. And also, a survey by Grenier et al. (2000) on the Tanzanian manufacturing sector could not draw inferences for de-industrialisation, but showed that the performance of the sector was reasonably good in the 1990s, with no evidence of de-industrialisation, despite a significant degree of trade liberalisation.

In the analysis of import trade in Uganda, Rudaheranwa (2000) argued that transaction costs, such as higher protection from natural trade barriers, transport and country location, are some of the reasons why the effects of trade liberalisation are often not observed, as they affect trade flows. He claims that evidence in their study does not support the argument that liberalisation leads to de-industrialisation. Sectors open to competition did not contract, but appeared able to increase efficiency (Rudaheranwa 2000). This argument supports the World Bank, who previously argued that available evidence suggests that countries that made large improvements in their macroeconomic policies had far exceeded rates of industrial growth than those that adjusted policies less intensively (World Bank 1994).

In other cases, like Ghana, decline in manufacturing industry was attributed to mismanagement of the economy, leading to shortages of foreign exchange and poor maintenance of equipment, including serious market distortions, as opposed to trade liberalisation (Tribe 2002). Tribe



presented evidence from Ghana and Uganda showing a strong recovery in manufacturing output between 1980s and mid-1990s as a result of capacity utilisation in existing industries. However, Tribe also points out that there is little evidence yet that trade liberalisation is associated with the positive transformation of the manufacturing sector.

In theory, openness and export oriented policies, and focusing on products where they have comparative advantages and with strong infrastructural support should yield positive prospects for the SSA countries in terms of enlarging the markets they serve. However, it has been argued elsewhere that the concept of IS, for infant industry, should not have been abandoned completely in the age of trade liberalisation and export-oriented development (Tribe 2000b). Tribe argues that export development is likely to be an integral part of industrial development in SSA and that some form of infant industry promotion in these economies is needed as otherwise de-industrialisation would be experienced due to competitive products from elsewhere. And this would be reflected in the poor performance of these economies.

On the other hand, John Thoburn (2002) argued that these countries could still use some short-term protection against imports in a positive way. He gives examples of the textile industries in Zimbabwe and Nigeria, where the industry has been protected against import competition. Thoburn argued that the textile firms have been able to use the protected home market as a base from which to export at least marginal supplies. He also gives an example of Indonesia where there is evidence that home market protection allowed firms to plan better and to take advantage of frequent periods when the world prices rose above the domestic price for particular textile products. However, Thoburn stresses that the concern is on how best to achieve the transition to a fully open economy and says:

There is no argument for long-term protection against imports. Once an economy is able to compete in world markets, there are great advantages to consumers of having free trade, and there are benefits to the economy more generally from imports of technology and investment goods that growing foreign exchange finance. However, premature opening to foreign competition without the establishment of a sound industrial base and market-supporting institutions is as likely to retard development as to promote it (Thoburn 2002: 286).

It had also, previously, been argued by Tribe (2000b) that since SSA countries are late industrialisers, there may be a possibility of stagnation of industrial growth, hence the need to put policies in place which would restrict some imports through tariffs and quotas in order to give the domestic infant industries a chance to get established. Tribe suggested that policy intervention measures could include public sector support for pre-investment or market studies, construction of



advanced factories, provision of industrial sites and manpower training and development and that such measures would help in the promotion of infant industry, at a vulnerable stage when they are just being established, in order for them to catch up with the rest of the world. He argues that:

Without any form of infant industry promotion sub-Saharan Africa countries might indeed suffer relative de-industrialisation due to inability to deal with the threshold or barrier problems at the point of establishment of new firms or plants (Tribe 2000b: 52).

However any form of government interventions would need careful definition and close monitoring to ensure that other well established firms do not take advantage. It should be noted that it is not clear cut that SSA industries' performance has been poor as a result of SAPs. Noorbakhsh and Paloni (2000) showed in their analysis, of SSA manufacturing industry performance, that there was an improvement in the share of manufacturing GDP, share of manufactured exports in total exports and average share of the countries' manufactured exports in world manufactured exports which they said were of little significance when the rate of growth of manufacturing was almost zero. Noorbakhsh and Paloni found no evidence that SAP caused de-industrialisation but argued that the negative results of SAPs in Africa may derive from the failures of the programme to take into account of other dimensions. They support the view that industrial development in SSA is more difficult than elsewhere due to poor infrastructure, insufficient human capital and entrepreneurship, small and fragmented markets (Noorbakhsh and Paloni 2000).

### **2.5.2 SSA: the SME sector under SAPs**

The continuing economic reform programmes implemented by many African countries have led to a rapid growth of small and micro-scale enterprises as private entrepreneurs take advantage of the relaxed economic environment. SSA countries adopted and implemented SAP measures at varying degrees and periods and over different lengths of times, and this would have varying effects on their economic and SME performances. Table 2.10 compares implementation of some structural adjustment measures in selected SSA countries, which would impact on poverty, trade and SME performance. As can be seen, some countries were already deeply engaged in the process of structural adjustment in the pre-1995 period (Ghana) while others (Tanzania) had barely started to implement it during that time. Such variation in economies means the importance of, composition and role of SMEs is likely to vary considerably and this will have to be taken into account when carrying out comparisons and by no means can one assume a priori similar impacts and reactions across all segments.



**Table 2.10: Selected policy measures in selected SSA countries**

	Ghana	Kenya	Malawi	Tanzania	Uganda	Zambia	South Africa
<b>Policy Measures:</b>							
Macroeconomic reforms (SAP/Economic Structural Adjustment Programme)	Yes pre-1995	Yes 1989	Yes 1987	Yes 1999	Yes pre-1995	Yes ..	Yes 1996
Reduction in cost of Business registration/licensing	Yes pre-1995	Yes 2000	Yes pre-1993	Yes 1999	Yes 1992	No n/a	No n/a
Effective rule of Law	Yes 2001	No n/a	Yes ..	No n/a	No n/a	Yes n/a	Yes 1996
Taxes lowered/simplified	Yes pre-1995	Yes ..	Yes post-1999	Yes ..	Yes pre-1995	Yes ..	Yes 1999-01
Removal of barriers to financial provision	Yes pre-1995	No n/a	Yes 1990-03	No n/a	Yes pre-1995	Yes ..	No n/a
Extensive privatisation	Yes pre-1995	No n/a	No n/a	Yes 1992	Yes 1996/98	Yes ..	No n/a
Simplified foreign trade procedure	Yes 1995	Yes 1992	Yes 1990-03	No n/a	Yes pre-1995	No n/a	Yes 1994/95/00/01

Source: World Development Indicators 1999, Policy Matrix Indicators, World Bank

.. = data not available

n/a = not applicable

However, it should be noted that, in general, adjustment programmes have done little to change Africa and allow greater integration into the global economy and manufacturing has been regressive for most of these countries (UNCTAD 2003c).

### 2.5.2.1 SAP impact on SME performance

Although the SAP was not formulated with SMEs or industrialisation specific in mind, its impact on the SME performance cannot be overlooked because, as discussed in previous sections, industrialisation and international trade will play an important part for integrating SSA into the global economy. Therefore, it is important to discuss how the SAP measures, such as financial liberalisation, trade liberalisation and public expenditure cuts have impacted on the performance of the SMEs, both directly and indirectly.



The policy environment faced by small enterprises determines, to a large extent, their ability to contribute to the process of development through growth in their numbers, size and productivity. 'Policies', in this case, refer to the rules that influence how resources are allocated (whether directly, through markets or in government budgets) and more broadly to government actions that affect people's capabilities and behaviour. Profitable investment may be lost because: policies are biased against small enterprises (for example difficulties in obtaining import licenses faced by small firms); market imperfections constraining small firm access to resources; and social and cultural mores inhibiting the participation of certain groups in small businesses (for example women). In the past, and to some extent now, policies have tended to favour large firms in terms of licensing permits, special concessions, obtaining credit from banks and tax incentives. Little et al. (1987) argued that up until the 1970s, most developing country governments had shown little concern for small-scale enterprises and that industrialisation was promoted through regulating trade, using investment incentives such as interest rate manipulation and credit control and undertaking public sector investments, all which discriminated against SMEs. Little et al. further argued that:

If there had been much concern for small-scale enterprises, ways might have been found to offset the disadvantages imposed upon them, even without the major change to a rather free-market economy which would have removed the bias caused by the trade and industrialisation regimes actually adopted (Little et. al 1987: p2).

Policy reform to correct such distortions and create a 'level playing field' would yield a more efficient allocation of resources and, quite likely, generate more employment and a more equal income distribution than a policy regime favouring large-scale capital-intensive investments. Most developing-country governments are now encouraging entrepreneurship and putting policies in place in order to develop their SME sectors, although to some extent the main aim is to relieve poverty and not necessarily for industrialisation purposes. A recent report by the Organisation for Economic Co-operation and Development (OECD) has argued that encouraging entrepreneurship and facilitating the rapid growth of innovative SMEs is an effective means of creating jobs, increasing productivity and alleviating poverty (OECD 2005a). The report further argues that identifying and implementing policies that can achieve these goals is becoming an increasing priority for governments of all types of countries.

Before discussing the SAP policy impact on SMEs, it is important to note that the order and timing of specific SAP measures also played a part on the impact and outcomes of the policy changes. The researcher has put together in Table 2.11 what some of the effects on SMEs could be when measures are sequenced inappropriately.



**Table 2.11 Impact of inappropriate sequencing of structural adjustment measures**

Measure	Measure Objectives	Possible impact on SMEs (direct and indirect)
Budgetary cuts in public spending, ahead of any other measures	To keep fiscal deficit low in order to avoid fuelling inflation.	This could prejudice services and infrastructure on which the government depends in order to stimulate export supply later on in the programme. The SMEs might not be able to expand their market share beyond their local boundaries due to high transport costs and poor communication roads hence not able to participate in global economic activity as there are no links.
Import liberalisation	To increase availability of intermediate inputs in order to encourage growth and development of manufacturing industry.	If carried out after currency devaluation, it is not of much use because if currency value is relatively low, SMEs may not be able to afford importing the inputs anyway. This measure might also increase competitive pressures on inefficient firms. Some of the SMEs may be inefficient because the infrastructural support system is not there in the first place.
Across-the-board trade liberalisation	In order to encourage outward-orientation of production and to enable increases in the efficiency of local output through greater competition.	If carried out before real depreciation, it could increase imports, which will out-compete domestic production (of import substitution consumer goods such as textiles, footwear) and lead to a rapid exhaustion of foreign exchange reserves. It may result in closure of some SMEs as they cannot compete against the cheaper imports, leading to unnecessary de-industrialisation (Riddell 1994). Without programmes that will increase technical, management & investment capabilities in the sector, trade liberalisation might work against them.
Currency devaluation	To raise the profitability of import substitutes as well as exports.	Without credit-support system in place for SMEs, devaluation makes it less affordable for manufacturing SMEs to import inputs of raw materials. This may also dampen overall demand.
Prices and Market Deregulation	To force supply and demand to become the determinant of prices in all markets, for efficient allocation of scarce resources.	If implemented before depreciation of the real exchange rate, profitability of traded goods does not increase, which is a disincentive to SME producers. Also, if carried out before public enterprise reform (privatisation), prices and markets remain monopolistic, which still discriminates SMEs.
Liberalisation of financial markets	To promote competition among financial institutions to make them more efficient and improve resource mobilisation, and also reduce rigidities that existed in allocation of credit by liberalising interest rates.	If there is no mechanism for providing credit to small industries, there will be inadequate credit available for promoting exports. And moreover enterprises borrowing at (commercial) high interest rates are likely to default.
Privatisation	Expected to foster efficiency, encourage new investment and free public resources for infrastructure and human capital investment.	If current managers of public enterprises have not got proper management and entrepreneurial skills beforehand, local entrepreneurs might not develop and not be able to manage the small enterprises efficiently.
Capital account liberalisation	To promote Foreign Direct Investment to complement local investment	This may not be successful if public spending has been cut considerably before hand such that there is: underdeveloped infrastructure, particularly transport & telecommunication; inadequate water & power supply. And also if this is carried out when an economy is not stable yet, and access to foreign exchange for importing inputs and capital goods is not properly in place, FDI might not be attracted.



As discussed before, despite the countries being recommended specific policy implementation sequencing, some did not necessarily follow these and were picking and choosing policies which they felt suited them and some of them still have not yet fully implemented these policies. As a result the impact on economic performance and SMEs would vary from country to country although the general consensus from the literature is that these policies have done more harm than good to the developing economies. For Malawi, the impact is further discussed in section 4.5.1.5, and indeed some of the policy impacts in Table 2.11 hold.

Even though trade liberalisation has a number of advantages in terms of its growth-enhancing potentials, there are a number of risks, which cannot be ignored. The exposure of domestic industries to competition from abroad as a result of trade liberalisation affects both SME owners and workers. As a result of increased competition, unless countries are able to match the productivity of their competitors or move into other products, the wages of their workers may be adversely affected. Manufacturing tends to be dominated by large companies in the formal sector where the wages in general tend to be higher than in the informal sector. And if the linkage between the informal and formal sectors is weak, as in many SSA countries, opening up of trade will accentuate the disadvantages of those employed in the informal sector.

Trade liberalisation, though expected to lead to greater competition and therefore increase firms' efficiency and give them greater access to intermediate inputs, has had some indirect impact on SMEs. From the Malawi experience, most SMEs have seen a quick way of making money by engaging in petty trading of cheap goods from China and other neighbouring countries, rather than engage in manufacturing themselves. The opening up of trade has resulted in influx of imports forcing some local manufacturing enterprises to close down because they are not yet well equipped to compete internationally (Malawi Government 2000b). This would of course be confirmed or disputed if it was possible to survey the failed SMEs themselves to find out if they attribute failure of their businesses to SAP.

SAPs have also impacted on SMEs, via the economic environment which has been created. For example cuts in public spending on infrastructure, whereby transport and communication system suffers, has seen some SME links to markets (both within and across country borders) being cut off thereby their market share reduced and hence not motivated to be innovative at all. Most of the developing countries have very small internal markets for manufacturers and access to external markets is vital, as has been the case for the developing Asian economies. However, it has been



argued that economic integration cannot guarantee enlargement of markets for industrial products (Sutcliffe 1971). Sutcliffe argued that, due to problems of transportation of goods within the developing countries, merely removing barriers to trade may not itself be an answer to enlarging the markets unless improvements are made to the transportation systems within and between countries.

Staley and Morse (1965) argued that in regions where transport system is poorly developed, products suited to the needs of local people should be the competitive bases upon which small producers should establish themselves in local niche markets. The small firms gain a larger relative role in developing countries, following demand associated with lower income levels, from markets segmented more by inadequate transport and communication. Thus the small firms largely serve small total markets. Staley and Morse suggested that where there are good local roads, regional firms should be able to achieve adequate delivery densities in moving goods to farms, construction sites and rural households, building a local position that withstands competition from distant firms (Staley and Morse 1965). This would however have implications for a country's internal trade as well as regional development. The products are favoured by local people and readily available and can compete successfully in domestic markets against imported goods, needing little or no protection, but by the same token possess little export potential.

In terms of financial liberalisation, banks have tended to operate largely as commercial enterprises with the aim of making profits and lending at market interest rates. This measure has had a direct impact on SMEs in that most of them cannot afford credit from the banks and they have no collateral to allow them to take up bank loans, furthermore there are not many other institutions set up to cater for SME financial needs. And also, in cases where countries have experienced high inflation rates through currency devaluations, SMEs have found it very expensive to purchase necessary input materials from other countries. Whether directly or indirectly, SAPs have been blamed for poor performance and, arguably, causing de-industrialisation in some SSA countries (Lall 1992, Stein 1992).

While acknowledging that SAPs alone cannot be totally blamed for the negative experiences of the SMEs in SSA, but by the fact that the relative prices and incentive environment changes, with the introduction of SAPs, this affects how SMEs behave and respond in order to prosper and survive in this new environment (Noorbakhsh and Paloni 2000). In addition it must also be noted that before the SAPs, SMEs were discriminated against by the import substitution policies which favoured large



monopolistic and state-owned enterprises. And further more, it may take time for the SMEs to realise the positive effects of SAPs, allowing for time lag between implementation and actual realisation of benefits, as seen from Table 2.10 most countries implemented SAPs, affecting business environment, from about mid to late 1990s. It has been shown elsewhere that there has been a fairly steady growth, on average, of the industrial sector in SSA during the 1990s (Tribe 2002).

#### **2.5.2.2 SME operating environment and experiences in selected SSA countries**

Table 2.12 draws data from 2003 firm-level surveys from seven different SSA countries, including Malawi, which have implemented similar macroeconomic changes and yet show different performances. 2003 survey data has been opted to be used in this case because it coincides with the time frame of the field survey work carried out for this study. The comparison between SMEs in different countries firstly reveals a variation in time required to start a business in the selected countries. In Malawi it takes a week longer than in the neighbouring Zambia to start a business but two and half weeks less than in Kenya. One explanation would be that since much more enterprises rely on bank financing in Kenya (28%) compared to 5% in Malawi, it is probably quicker to start a business with internal funds than in situations like Kenya where a bigger number has to wait for a bank's decision. Nevertheless it still takes longer in Benin than Malawi to start a business and yet they both heavily rely on internal financing, hence there could be other reasons for the differences in times. The table also reveals that obtaining finance to start a business is difficult for most SSA countries whose small enterprises indicated that less than 15% obtain financing from banks with the exception of Kenya where it was 28%. This reflects the poor development of the financial sector for most of them.

Corruption is also of concern for most of these countries. The data reveals that over 30% of enterprises in the majority of the countries have to pay a bribe of some sort to get things done, reaching as high as over 70% in Kenya. Kenya, Mali and Zambia are the most corrupt on that front in comparison to 22% in Malawi. The data also indicates that Tanzania, Malawi, Kenya and Uganda have low capacity utilisation. Low capacity utilisation can indicate demand constraints or lack of availability of inputs on the supply side. For Malawi, a small market size with low purchasing power is the most likely reason for the low capacity utilisation. Quality of infrastructure plays a crucial part in firm productivity. The surveyed enterprises in Malawi reported about 76% loss of sales due to power outages, the highest of most of SSA countries. Out of the domestic sales, none are sold to Multi-National Companies (MNCs) in Malawi, and very small percentages for the other



countries with the exception of Zambia's small enterprises which sell 19% of their domestic sales to MNCs. None of the surveyed small enterprises in Malawi exported directly compared to the 22% of neighbouring Zambia and 28% of Kenya (Table 2.12).

**Table 2.12: SME characteristics, comparison of selected SSA countries, 2003**

	Benin	Kenya	Malawi	South Africa	Mali	Tanzania	Uganda	Zambia
Time required to start a business (days)	63	60	42	38	42	35	36	35
Expected to give gifts to get operating licence (%)	40	..	0	0	8	16	3	..
Expected to give gifts to get import licence (%)	37	0	..	0	3	6	0	..
Pays bribes to get things done (%)	60	71	22	2	58	30	32	50
Business Financing:								
Internal financing (%)	85	48	83	67	89	82	87	65
Bank financing (%)	5	28	5	13	4	4	2	9
Informal financing (%)	3	3	7	2	1	4	3	2
SMEs using web interaction with clients/suppliers (%)	14	14	6	53	17	5	2	30
ISO Certification ownership (%)	0.75	..	0	25	1	2	..	13
Capacity utilisation (%)	58	55	53	75	72	51	56	59
Skilled production workers (% of workforce)	52	27	21	41	46	53	22	28
SMEs Spending on machinery/equipment (%)	9	4	3	6	9	21	3	17
Average time to claim imports from customs (days)	8	8	..	5	8	17	..	5
Domestic inputs (% of inputs)	72	..	66	76	54	83	86	49
Imported inputs directly (% of inputs)	13	..	17	18	18	7	6	40
Firms importing directly (%)	28	..	24	38	21	18	10	57
Firms exporting directly (%)	8	28	0	31	9	6	6	22
National market share (%)	11	16	11	25	18	12	16	23
Domestic Sales (% of total sales)	95	90	100	92	95	96	98	85
Customers, % of domestic sales to:								
Government	10	2	8	5	5	5	4	8
MNC in the country	4	5	0	7	4	2	5	19
Larger domestic firms	14	19	11	41	7	7	13	20
Other small firms/individuals	66	66	81	45	81	83	73	39
State-owned enterprises	5	6	..	3	3	3	4	13
Share of net profits re-invested in the last year (%)	51	46	52	92	38	37	33	71
% Value of sales lost due to electricity outages	7	11	76	0.7	1	10	4	4

source: World Bank, Doing Business 2003b

.. = data not available

When comparing the top ten constraints to business productivity or growth, the data revealed that cost of finance/access to finance ranked in the top three constraints for most of the SSA countries. Tax rates/administration and corruption featured high as well for most of them and the data shows that in general most enterprises in that region face similar problems. However, enterprises in



Malawi largely consider macroeconomic instability as the greatest obstacle to their operation and growth compared to Kenya and Tanzania which ranked this constraint as sixth (Table 2.13).

<b>Table 2.13:Top Ten Constraints (identified by small enterprises as major or very severe ), selected SSA countries, country ranking of problems</b>								
	Benin	Kenya	Malawi	South Africa	Mali	Tanzania	Uganda	Zambia
Cost of finance (interest rates)	4	2	2	6	1	3	1	1
Tax Rates	1	3	5	7	5	1	2	3
Macroeconomic instability		6	1	2		6	3	2
Access to finance (collateral requirements)	3		3	5		2	4	
Electricity	6	8	4		7		5	7
Corruption	5	1	8	10	2	5	6	6
Tax Administration	2	7	10		6	4	7	
Anticompetitive of informal practices		4			3		8	
Skills & Education of available workers		5	6	1	9	9	9	9
Regulatory policy uncertainty	7			8	10	8	10	4
Customs & trade regulation	8	10		9		7		
Crime, theft & disorders			7	4	8	10		5
Transport			9					
Access to land					4			
Labour regulation				3				
Business licensing & operating permits	9							
Telecommunications		9						10
Legal system	10							8
<b>Source: World Bank, Enterprise Surveys 2003c</b>								

In addition to these internal constraints, there are external forms of constraints, such as market protection of developed countries, in the form of 'regulations' discussed earlier. It appears that although trade policy reforms have led to falling tariffs, they have led to growth of new forms of protection. As discussed in section 2.4.1, 'Standards' are being required and this has particular implications for SMEs. One might question whether the same typical categories used for large companies should be applied in case of SMEs or if they need specific standards as management in SMEs is often informal and they lack resources and technical skills.

Standards, whether in processes or products, are becoming an increasingly important qualifying requirement for participating in the global product markets and global value chains. Suppliers of TNCs (including SMEs) are required to meet certain global quality standards in order to satisfy customers. Thus, the demand for standards comes from both final buyers and TNCs controlling the global production systems. The problem for SMEs is that the cost of compliance can be quite high as they will need to develop capabilities to serve the TNCs. As well as gaining from the transfer of



new technologies and capabilities, those SMEs operating within the supply chain of multinational companies can benefit from greater market opportunities. It has been argued that alliances are prevalent in global oligopolies, serving as vehicles for the transfer of technology between firms, achieving economies of scale, building technical skills and accessing markets, skills and resources (Yoffie 1993).

There are issues with the entrepreneur skills and management strategies which also play a significant role in the performance of SMEs. From these discussions it can be said that while macro-economic policies, such as trade liberalisation, are important in creating the pre-condition for growth, they may not be sufficient. There is evidence that efficiency with which firms operates is important in understanding whether they can be successful exporters (UNIDO 2001a). SME managers in SSA countries have been described to lack the technical and management capability to respond to new relative opportunities (brought about by trade liberalisation) and to adjust their utilisation of capital, labour and intermediate inputs to minimise cost and increase supply (Lall 1992). Managers and workers of these countries will have to learn to use new technologies efficiently by the standards of industrial countries, and this takes time, as it is a process of learning by doing. Therefore, in addition to the SAP policies, there is a need for policies which improve efficiency at firm-level. A similar argument also applies for finance and market. Entrepreneurial skills and proper business strategies alone are not enough if the market is not there and if there is not enough finance to run the business and market the products. In the age of economic globalisation, all these factors inter-link and impact upon the performance of the SMEs.

The Problems of SMEs often directly relate to their size which makes it difficult for them to acquire good quality inputs cheaply, enskill their workers, gain access to finance required to serve distant markets and to expand their operations and to acquire the required technology. However this could be overcome when they cluster together in order to benefit from collective efficiency. Working together with other enterprises, through networks and corporation, SMEs can benefit from economies of scale and economies of scope and thus can overcome their disadvantage of smallness. For many years, inter-firm cooperation has been discussed as a corporate strategy, but it has become more important in recent years (Lawrence et al. 2002, Schilling 2002, Silverman and Baum 2002). Cooperating with other firms provides many advantages, especially access to scarce resources like new technologies, products, skills and know-how that will not be otherwise available (Narayanan 2000, Silverman and Baum 2002).



## **2.6 Recent International Policy Developments: post-SAPs**

Neo-liberal adjustment policies are still a key part of the WB and IMF conditions for lending funds although a new policy grouped under the name of Poverty Reduction Strategy has emerged in recent years. Governments of these poor countries are required to produce a Poverty Reduction Strategy document in order to qualify for funding and working towards forgiveness of some of the debts. The World Bank and IMF launched the 'Heavily Indebted Poor Countries' (HIPC) initiative in 1996 and an extension of it called the Enhanced HIPC initiative in 1999. The initiative had an initial list of 42 countries, Malawi included, and aimed to offer some sort of way out of the burden of unsustainable debts.

The HIPC includes three distinct stages (Figure 2.13). Firstly, countries have to qualify for the initiative, by having debt levels which the WB and IMF define as 'unsustainable', and this is the pre-decision point. Secondly, countries have to prepare an interim Poverty Reduction Strategy Paper (PRSP) and reach a 'decision point', at which they begin to receive debt relief. In the third and final stage, countries are required to prepare a full PRSP, based on consultations with civil society organisations and donors, in order to promote a participatory approach to national development (World Bank 2004b). They also have to comply with numerous trigger conditions, including implementation of an IMF Programme, which is nothing new considering that the conditionalities are not far off from those of the SAP. At the end of this stage, they reach a 'completion point' where a portion of their debts would be finally cancelled.

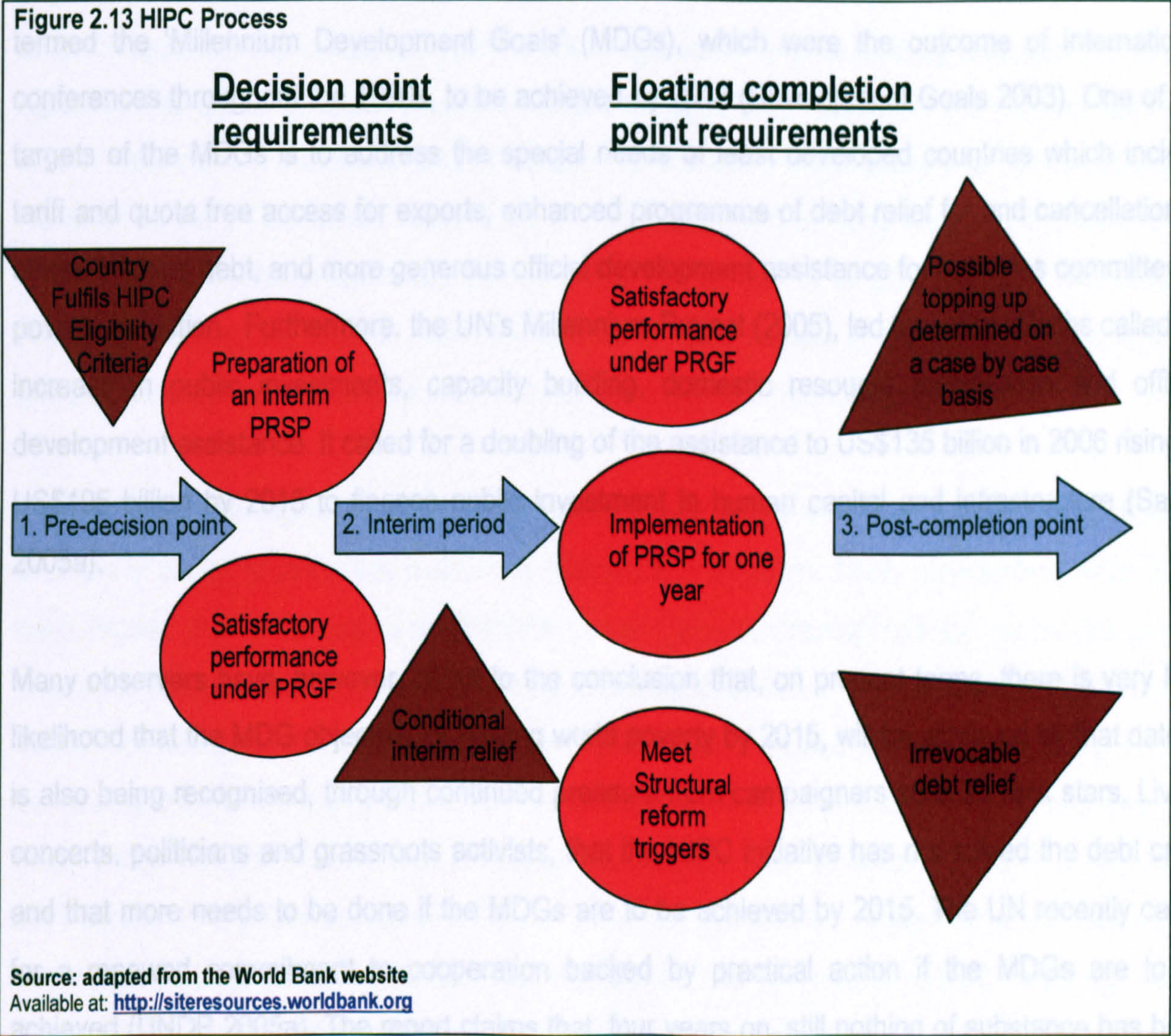
The underlying hypothesis for PRSPs had been that the SAPs were missing a crucial ingredient, national ownership. Although the PRSP initiative itself came from Washington, it was believed that PRSPs would enable a new type of partnership between recipients and donors, with the recipients taking the lead (World Bank 2000b). The Overseas Development Institute has been at the forefront of the research and policy debate, regarding PRSPs, from the start and has been offering many insights on the experiences with the PRS process, summarised by Booth (2003a). Drawing on evidence, on study of PRSP experience, from seven SSA countries (Benin, Ghana, Kenya, Malawi, Mali, Rwanda and Tanzania), David Booth (2003a) concluded that ownership on the first dimension was low in all cases. Booth (2003b) argued that low-levels of 'national ownership' may affect policy effectiveness and sustainability.

It has also been argued elsewhere, that although consultation processes have occurred in the formulation of the PRSPs, the voice of marginalised groups has been very limited, hence it has



been said that the PRSPs are not very much different from SAPs (Bradshaw and Linneker 2003, Power 2003). The fact that the initiative itself came from Washington, seemed to have been seen as a problem. Booth argued that the PRSP initiative and incentive put in place around it had not yet been sufficient to generate full national ownership, even in terms of the process. He further argued that the most critical dimension of national ownership would be the mainstreaming of poverty reduction, in the sense of articulating the goals of the strategy with budget, and then using budgetary incentives to force Ministries and districts to pay attention to them (Booth 2003b).

Figure 2.13 HIPC Process



Following on the HIPC initiative, it was reported that by 2003, only eight countries had so far received substantial debt write-off under HIPC and that the programme was failing to restore countries to debt 'sustainability' even after completing their passage through HIPC. However, on the positive note, it was reported that the HIPC initiative had reduced annual debt servicing for 26 countries by an average of 40%, although not shared evenly (Greenhill et al. 2003). In June 2005, a group of eight wealthy countries (G8) proposed that the three multilateral institutions, IMF,



International Development Association of the WB and the African Development Fund, cancel 100% of debt claims on countries that had reached completion point under the IMF/WB HIPC initiative.

Although it is highly unlikely that significant further progress on low-income country debt has been made by now (2006), at least 'aid' and 'poverty' are back on the global agenda. In recent years there has been general consensus about the urgency of poverty reduction in the developing economies and the importance of more and better aid to combat poverty. In September 2000 at the UN Millennium Summit, the UN agreed to adopt a set of eight objectives incorporating targets for reducing poverty and other sources of human deprivation and promoting sustainable development, termed the 'Millennium Development Goals' (MDGs), which were the outcome of international conferences throughout the 1990s, to be achieved by 2015 (Development Goals 2003). One of the targets of the MDGs is to address the special needs of least developed countries which include tariff and quota free access for exports, enhanced programme of debt relief for and cancellation of official bilateral debt, and more generous official development assistance for countries committed to poverty reduction. Furthermore, the UN's Millennium Project (2005), led by Jeffery Sachs called for increase in public investments, capacity building, domestic resource mobilisation and official development assistance. It called for a doubling of the assistance to US\$135 billion in 2006 rising to US\$195 billion by 2015 to finance public investment in human capital and infrastructure (Sachs 2005a).

Many observers have, however, come to the conclusion that, on present terms, there is very little likelihood that the MDG objective, of halving world poverty by 2015, will be achieved by that date. It is also being recognised, through continued pressure from campaigners such as rock stars, Live 8 concerts, politicians and grassroots activists, that the HIPC initiative has not solved the debt crisis and that more needs to be done if the MDGs are to be achieved by 2015. The UN recently called for a renewed commitment to cooperation backed by practical action if the MDGs are to be achieved (UNDP 2005a). The report claims that, four years on, still nothing of substance has been achieved. Rich country trade policies continue to deny poor countries and poor people a fair share of global prosperity and that limiting the potential through unfair trade policies is inconsistent with a commitment to MDGs. The Department of Trade and Industry of the British Government, in its white paper, pledged to a commitment to make trade work for the MDGs (DTI 2004) and to assist the developing countries to seize the opportunities and manage the threats from increasing globalised markets. The DfID pointed out that it is encouraging that trade is being better integrated into countries' poverty reduction strategies (DfID 2005a).



Another policy initiative that has created hot debates at trade talks at the WTO ministerial annual meetings has been the issue of trade protectionism against the developing countries by the North. The trade negotiations seriously started with the Doha Development Agenda, at the 4<sup>th</sup> WTO ministerial meeting in 2001, with a promise of reducing agricultural subsidies in developing countries and tearing down the trade barriers that hinder market access for African goods, within a negotiated multilateral framework. Progress so far has been very limited, especially on agricultural liberalisation. Although one of the WTO's remits is to promote freeing up of trade between members, it has been criticised for being influenced by the views of Northern countries at the expense of the South. In September 2003, at the WTO meeting in Cancún, Mexico, the focus was on the inequalities in protectionism, particularly in agriculture and the meeting collapsed without any agreement as some Southern countries refused to agree on proposals of the US and European Union. Failure of the Ministerial talks in Cancún represented a major setback for African countries. However, at the 6<sup>th</sup> Ministerial Conference, in December 2005, in Hong Kong, an end-date (2013) for all export subsidies in agriculture and solid duty-free access for 32 LDC members was secured. And also, recently, the WB has called for removal of trade barriers in rich countries, and for more effective development assistance in order to correct inequality (World Bank 2006a).

There is a general agreement that development is not simply economic growth but also critical changes in social relations and institutions (Barnes and Sheppard 1992, Nicholaides 1992). It has been argued that if development conforms to neo-classical prescriptions for market-led growth, unrealistic policy recommendations are likely to be made, as has been the case for SSA (Winiecki 1993). The neoliberal development strategies have so far produced disappointing results in many developing countries. Poverty has remained widespread while emphasis on market openness has made states vulnerable to the side effects of globalisation, such as surging flows of private short-term capital. In a policy document by Burki and Perry (1998) they argued for going beyond the 'Washington Consensus'. They implied that the reforms had not been effective in reducing poverty and inequality and argued for the need to focus on improving quality of investments in human development, promoting development of sound and efficient financial markets, enhancing legal and regulatory environment and improving the quality of public sector. The IMF has also confirmed that growth has been disappointing and that the reforms were uneven and remained incomplete (Singh et al. 2005). Krueger (2004) also expressed failure of these reforms, which she said were meant well, tried little and failed much. In 2005, the World Bank produced a report which emphasised the need for humility, policy diversity, selective and modest reforms and experimentation (World Bank 2005d). Some of the neo-liberal policy failures noted in the report were: the collapse in output in



countries making transition from communism to market; frequent financial crises in Latin America, East Asia, Russia and Turkey; the Latin America recovery of the first half of 1990s was short-lived; and SSA failed to take off despite strong policy reforms, improvements in the political and external environments and continued foreign aid.

The general consensus is that things have not worked out the way they were intended, and now analysts/economists are thinking of what should replace the 'Washington Consensus'. It has been suggested that a 'post-Washington Consensus' be endorsed, comprising an expanded reform agenda emphasising crisis-proofing economics, second regeneration reforms and policies addressing inequality and social issues (Kuczynski and Williamson 2003). It seems that, while the Washington Consensus provided a good mixture of reforms to both stabilise the economy and encourage private sector activity, it did very little to help resolve structural and institutional constraints on growth. The emphasis is now on the need for governments to ensure that strong domestic institutions and policies are in place before opening up their economies to flighty foreign capital (Easterly and Levin 2003, Rodrik et al 2004).

Another World Development Report has focused on what governments can do to improve the investment climates of their societies in order to increase growth and reduce poverty (World Bank 2005b). The report argued that a good investment climate is central to growth and poverty reduction and a viable private sector creates jobs, provides goods and services needed to improve living standards. The reports went further to say that too often governments stunt the size of those contributions by creating unjustified risks, costs (such as weak contract enforcement, corruption, crime, unreliable infrastructure and inefficient regulation) and barriers to competition. Development is not good without a good investment climate and a buoyant private sector hence the Bank's first pillar of the overall strategy for poverty reduction is improving the investment climates of these economies (World Bank 2005b). It is believed that increase in political pluralism combined with greater unity among donors looks positive for continuation of Africa's growth recovery and that political freedom will enhance the environment for capital accumulation and growth (Ndulu and O'Connell 1999).

Many other organisations and individuals agree that all the efforts and initiative so far have not been enough and are not progressing at a quick enough pace to help masses of people who are in desperate need of poverty alleviation and that many countries are still burdened with debt that they cannot do anything for their own people. That is why in 2004 a UK alliance of charities, trade unions, campaigning groups and celebrities, under the name of 'Make Poverty History', was



launched to drive forward the struggle against poverty and injustice. The Make Poverty History (MPH) manifesto document calls for urgent policy changes on three critical and linked areas: trade, debt and aid (MPH 2005). The document calls for the rich countries to end export subsidies that damage the livelihoods of poor rural communities around the world and that 'trade justice' and not 'free trade' is needed. It also demands that the IMF and WB stop forcing poor countries to open their markets to trade with rich countries as this is obviously not working. On the issue of debt, MPH requested that debt of the developing countries be cancelled in full by fair and transparent means and that the IMF and WB stop making these countries jump through hoops in order to qualify for debt relief. As regards to aid, the document pointed out that more international aid is required and proposed that at least US\$50 billion per year be delivered in order to eradicate poverty and that focus should be on people's needs (MPH 2005).

In addition to the MPH manifesto document, July 2005 saw the biggest ever anti-poverty movement under the banner of 'make poverty history'. It is believed that over 225,000 people took to the streets of Edinburgh to call on world leaders to act at the G8 summit and demanded action to end poverty. Rich countries responded to this mass movement by agreeing to cancel most of the debt of 40 poor countries and promised US\$50 billion more aid by 2010 (Oxfam 2005). Following that, in December 2005, the IMF in its press release announced a 100% debt relief for 19 countries to take effect early 2006 and these countries would be monitored under the Multilateral Debt Relief Initiative (IMF 2005b). It should be noted that, at the time, Malawi was not amongst those 19 countries as it was not qualified yet. However the G8 are yet to deliver on their promise of a trade deal that works for the world's poorest people. No new financial commitments were made at the 2006 G8 summit in St. Petersburg and there were no serious offers by the USA and Europe to poorer countries on trade.

## **2.7 Summary**

The IMF and World Bank have been playing a key role in African economic policies ever since the late 1970s (Elbadawi 1992). These institutions have in fact by now gained an unprecedented and pervasive influence over policy-making in African countries, which has obviously stimulated a lively and at times very heated debate in academic and policy-making circles. Colonialism subordinated SSA's development to the needs of stronger economic centres and nothing seems to be any different now. It has been suggested elsewhere that the successor to post-colonial sovereignty is the neo-colonial vassalage in which the Western powers assume direct and open-ended control over the administration, security and economic policies of deteriorated states under the banner of



the United Nations and various donors (Plank 1993). Africa finds itself in a situation, shaped by both its long established weaknesses and by the terms of its current subordination where it is forced to slot into the role defined by capital and its functionaries beyond its borders. Under the existing global capitalism, debt, market liberalisation as a condition of aid and predatory outside forces are part to the continued marginalisation of SSA.

As regards to trade liberalisation, the effects are not agreed and certainly are not uniform for all places and times. Developing countries feel that they have not been given enough market access in developed countries and they contend that there are still many tariff and non-tariff barriers in the North to the potential exports of the developing countries. Industry has not developed in most of these countries. Apart from SAPs, there are also other reasons given for the failure of the industrial development in SSA which include poor infrastructure, insufficient human capital and entrepreneurship, small and fragmented markets, geography and natural resource endowments (UNIDO 1996). As regards to de-industrialisation, there is still debate about whether it is due to open competition resulting in displacing inefficient industries or due to lack of competitiveness whereby Asian economies are penetrating African markets making SSA open trade policy too little too late (Belshaw and Livingstone 2002).

Despite all the policy changes over the years, the problem of mass poverty persists and is once again to the forefront of political agenda. More recent international debates and negotiations suggest that a new stage has begun. Although all these debates and negotiations have been going on, for several years now, at the WTO Ministerial annual Conferences, no significant progress has been made in terms of any notable changes in the lives of the poor or being able to access developed countries' markets. External debt also continues to be one of the major obstacles to the development efforts of Africa. In spite of the HIPC initiatives, Africa still remains the most indebted continent relative to its growth national income and still faces the danger of being left behind by the rapid changes being brought about by the forces of globalisation.



# Chapter Three

## Research Methodology

### 3.1 Introduction

This chapter discusses the overall approach to studying the research topic and particular research techniques which have been employed and adapted. All the methodological issues such as population coverage, information sought, how this information was collected, how it was processed and interpreted, including reasons for the chosen research techniques and rationale are also discussed. The study approach, methods and other design decisions have been guided by the research objectives specified in Chapter One. The Conceptual Framework presented in Figure 1.1, Chapter One, was viewed as the map of the territory being investigated and the focus of the research originated from the literature and theoretical concepts discussed in Chapter Two. The framework links concept to empirical data, and deductive reasoning was used to move from the large context of theory to generate the specific questions in the questionnaire (Appendix 7).

As the central theme of this study concerns consequences of globalisation and economic reform measures, on the development of the SME sector in Malawi, the researcher came up with the following basic questions to aid in developing the research objectives outlined in Chapter One:

- *How have the SAPs, in particular trade liberalisation, and globalisation impacted on small and micro scale enterprises in Malawi?*
- *How have the SMEs responded to the adjustment measures?*
- *What sort of inter-firm relationships have emerged as a result of competition?*
- *Is the new economic environment of 'free trade' favourable or not for sustained growth and development of the SME sector?*
- *Is there an alternative strategy for developing the sector and what can the internal and external institutions do in order to achieve global economic integration rather than marginalisation?*

After examining and refining these questions, the aim and the objective statements, outlined in Chapter One, were clarified and were thought to be researchable and worth investigating. The questions were formulated as a way of explicating any theoretical assumptions and orienting the researcher to the research objectives. The objectives had direct implications for the choice of methodology and tools that were used to obtain the information.



It was decided not to hypothesise the objectives due to the smallness of the research and it was felt that it was not necessary to carry out a statistical testing of hypothesis as often required with large-scale sample surveys. A precise statement of objectives was thought to be quite sufficient, as long as it was clear on how and what was being investigated. The objectives had direct implications for the choice of methodology and tools that were used to obtain the information. The researcher is confident that the methods opted for and discussed in the following sections helped in meeting the research objectives.

### **3.2 Study Approach**

The empirical research work was carried out in two phases: Phase I involved informal interviews with key people in both governmental and non-governmental organisations; and Phase II involved structured interviews with entrepreneurs. Phase one was a fact finding exercise at policy level whereas phase two was the main survey on entrepreneurs. A positivistic approach to data collection in the second phase of the study as opposed to humanistic approach where human judgment, perception and emotions play important role, was adopted. The research had all the characteristics, of 'positivist' approach, as set out by Tribe and Summer (2004): the goal was to seek out the truth or reality, regarding how SMEs in Malawi have been affected by globalisation and SAPs, through empirical evidence; the researcher was independent of the researched and was objective; and although there was some qualitative information gathered, the research was predominantly quantitative. Positivist is identified with structured approach and power inequalities between the researcher and the researched. The approach was structured in a way that the respondents were given the power to discuss and inform what they thought and how they felt the SAPs and globalisation had affected their SMEs.

This study was regarded as a social research and as such it involved 'engaging' with the world. In simple terms, social research is a way of finding answers to such questions as 'what is happening', 'why is it happening' and 'how does that affect people'. Blaikie defines social research as 'exploring, describing, understanding, explaining, predicting, changing or evaluating some aspect of the social world' (Blaikie 1993, p.4). This view is supported by Gilbert (2001) who notes that social research should not only be concerned with a descriptive 'fact gathering' exercise but with understanding the social situation in which researcher is involved, and it has to be located within an academic discipline which offers perspectives and methods. Gilbert (2001) prescribed three ingredients to social research: construction of theory; design of methods for gathering data; and collection of the



data, and these are the steps which have been followed in this study. The three stages in relation to this study have been discussed in the following sections.

### **3.3 Theoretical Context**

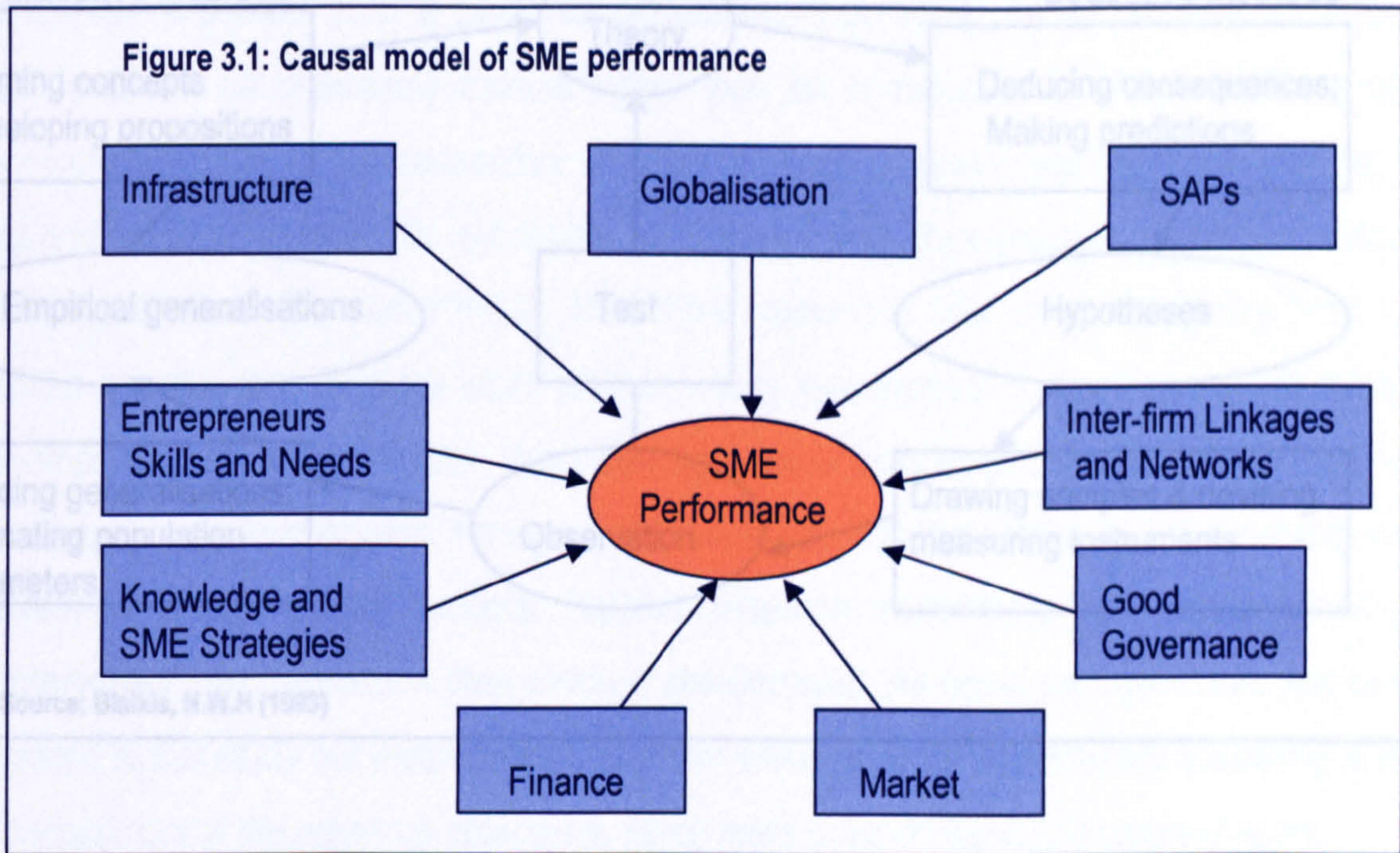
This section sets out the theoretical assumptions, which underlie this study. Even carefully collected results can be misleading if the underlying context of assumptions is wrong. The conceptual context is a key part of the study design and presents the theory behind this research. Theory links together elements in a causal process to produce a more general explanation of particulars that have to be observed. The conceptual framework discussed in Chapter One argues, on the one hand, that SME performance and competitiveness would improve and SSA be more integrated in the global economy if SAPs were applied, and on the other hand attributes marginalisation of SSA economies to SAP measures, in particular trade liberalisation. As seen from the discussions in Chapter Two, some analysts have argued that due to trade liberalisation, sub-Saharan Africa is being integrated into the global economy whilst other analysts claimed that it is being marginalised even more.

Figure 1.1 in Chapter One presents, diagrammatically, the main issues and key factors, concepts or variables being studied and the presumed relationship among them. However, the explanations of the relationship between the concepts should not be considered as mutually exclusive because theory is multi-causal. Thus, as discussed in Chapter Two, as well as the SAPs impacting on SMEs, there are other factors which are not directly associated with SAPs such as infrastructure, geographical location, social characteristics, education levels, entrepreneur business management skills, business strategies, marketing skills, type of products being merchandised, which also impact on the performance of SMEs. Therefore this research also includes analysis and integration of these other variables.

Figure 3.1 presents a simplified causal model of SME performance and it should be noted that the factors are not exhaustive. Analysis and discussion of the entrepreneur survey in this study integrates these causal factors in studying the impact of globalisation and SAPs on the SMEs in Malawi. International trade theory assumes that increased openness to trade will lead to more integration and that is why the 1980s saw a significant shift in development policies from state-led to market-led. It has been argued from the discussions in the literature that just opening up of an economy is not enough. The model of international trade assumes that there is full employment of all factors of production, which is least realistic in SSA countries and that economies have equal



influence in their trade with each other. In reality there is unequal exchange between primary producing underdeveloped economies and products of the advanced industrial economies.

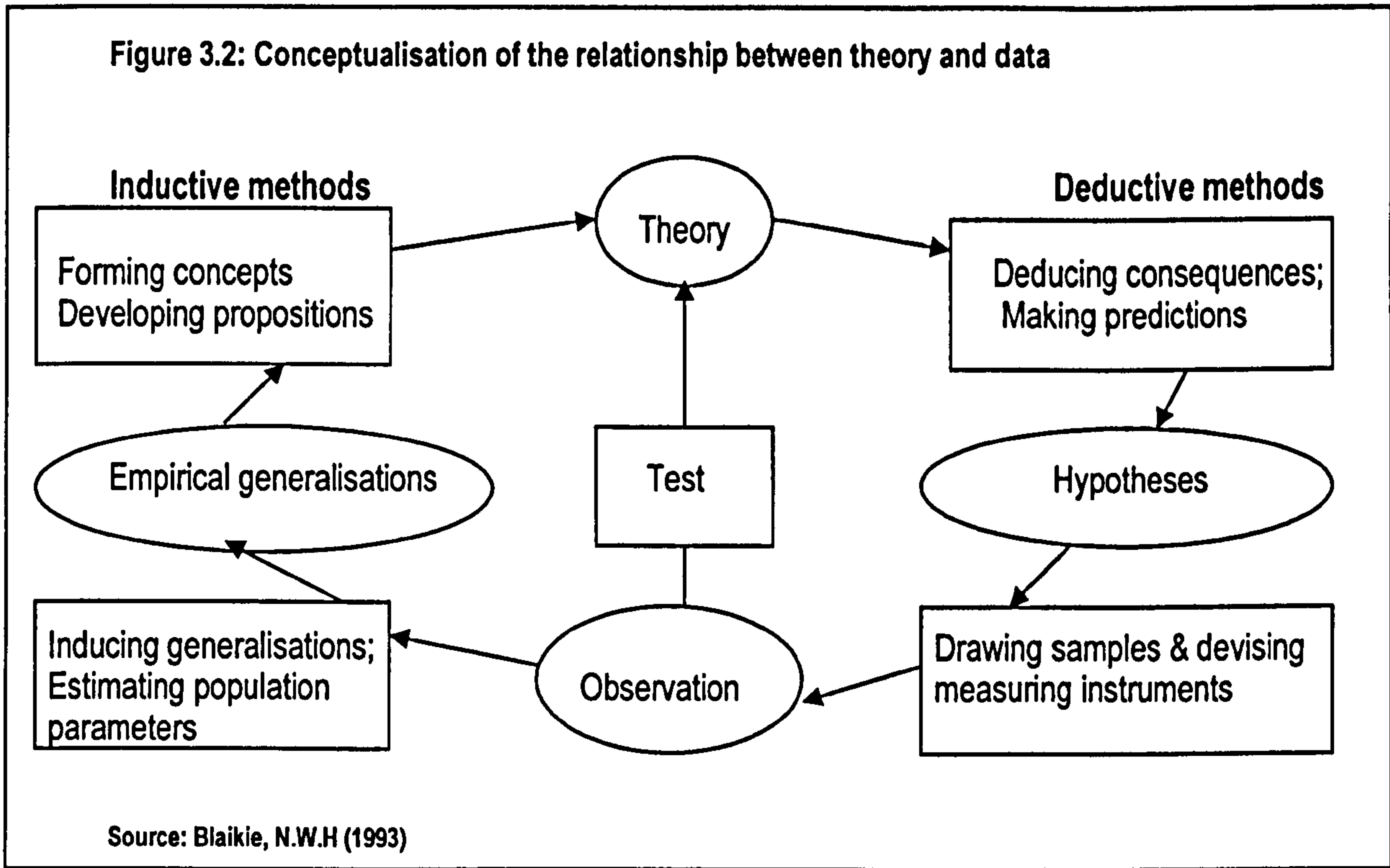


This study attempts to link the ‘open-market leads to global integration’ theory and SME performance to the data evidence gathered from Malawi. Before discussing the methods for gathering the data, the relationship between the theory and data is discussed.

### 3.3.1 Linking Theory to Evidence

Theory comes partly from evidence and partly from beliefs and ideas, and some research intends to find evidence to back the theory up or otherwise. In this study, all the theory has come from Literature, and the theoretical perspectives of previous work cited in the literature review form the research context. In order to find the evidence to support the analysis of the impact of SAPs and globalisation on SMEs in Malawi, within the discussed theoretical context, data was required. Wallace (1971) presented a diagrammatic conceptualisation of the relationship between theory and data (Figure 3.2). The model brings together elements of induction and deduction through a process of moving from observation to theory and from theory to observation. It is possible to enter the scientific cycle at any stage, with hypotheses, observation, empirical generalisation or theories, but each is connected to the others. On the inductive side of the model, researcher develops theory out of the descriptive and interpretive process whereas on the deductive side, researcher builds a study out of an established theoretical framework. In this research, a theoretical framework, from which this study is built, was established through a deduction process to begin with.





Some writers recommend a mixed strategy, of quantitative and qualitative research methods, in studying the relationship between theory and data (Brannen 1992, Creswell 2002). These research methods are often best used to address different questions and purposes and the split between the two methods is no longer as obvious as it used to be since more and more studies are now using multiple research methods in their studies than before. As discussed in section 3.2 the overall approach to this study was positivistic and the main (second phase) survey was predominantly quantitative (one of the characteristics of positivist approach). However, during the first phase (fact finding phase) of the study the data collected was qualitative.

The strength of qualitative research method derives primarily from the inductive approach, its focus on specific situations or people and its emphasis on words rather than numbers. The method typically involves studying a relatively small number of individuals or situations and preserves the individuality of each in analysis rather than collecting data from large samples and aggregating the data across individuals or situations. It is suited for understanding the meaning, situations and actions for participants in the study and accounts that they give of their experiences. This helped the researcher to try and understand part of the reality. This method helps in understanding of how participants make sense of events and how their understandings influence their behaviour. It is also suited for understanding the particular context within which the participants act, and the influence that this context has on their actions



Issues of theory and evidence also lead to considering how 'objective' or 'detached' one should be in research work. It has been argued that observation of facts is not straight-forward and involves some subjectivity and interpretation for example in deciding which categories responses should fall in. Wallace (1971) argued from a positivist standpoint, that social reality is open to outside observation and can be objectively studied rather than be constructed by the perceptions and experiences of its members. The researcher adopted as much objective procedures as one can in describing and explaining the reality 'out there', and through deductive process, theoretical notions guided the observations that were made. Deductive reasoning was used in arguing from the general to the specific, thus from the wider problem being investigated to specific concepts related to one another through causal model. Such concepts were then operationalised into indicators. Thus the unseen were investigated through variables which are observable and measurable and then interrelated through causal models. Reliable research instruments were designed which reduced interviewer bias to produce data which is standardised. As noted, no hypothesis has been made or tested in this study but instead the researcher came up with researchable questions within the SAP context, out of the research objectives, which were used on surveyed entrepreneurs.

From the surveyed entrepreneurs, observations were made and parameters estimated, thus moving towards the inductive side of the model. Inductive research begins with specific observations and moves towards the development of general patterns that emerge from the subjects under study. The induction appears solid because it is grounded in 'facts' and therefore empiricist and has been used because it fits in with this study, evolving from researcher's experience to literature review and then to field study. The cycle was entered at the theory stage through forming concepts where the study has been built out of a conceptual framework. From the empirical findings (evidence) consequences were deduced. The impact of SAPs was measured by analysing information and opinions gathered from the entrepreneurs.

There have been some debates in the literature regarding the methods use in measuring the impact of SAPs and flaws in the approaches have been pointed out. Howard Stein, in his paper, discussed five methods, which can be used in assessing the impact of structural adjustment: the 'before and after' method, the 'control-group' approach, the 'modified control group', the 'decomposition' method and the 'with and without' simulations (Stein 1999). The first compares the changes in the mean value before and after adjustment to see if there are statistically significant changes. The second compares macro-economic performance variables for programme and non-programme countries. The third approach is same as the second only that it attempts to control for differences in the external environment and initial conditions when comparing programme and non-



programme countries. The fourth method uses econometrics to test the relationship between specific policy changes and outcome by pooling data of countries undertaking quantitatively similar measures, whereas the fifth approach relies on Computable-general-Equilibrium (CGE) simulations and Social Accounting Matrix (SAM) models and uses more structuralist assumptions. Stein points out how flawed these methods are and argues that:

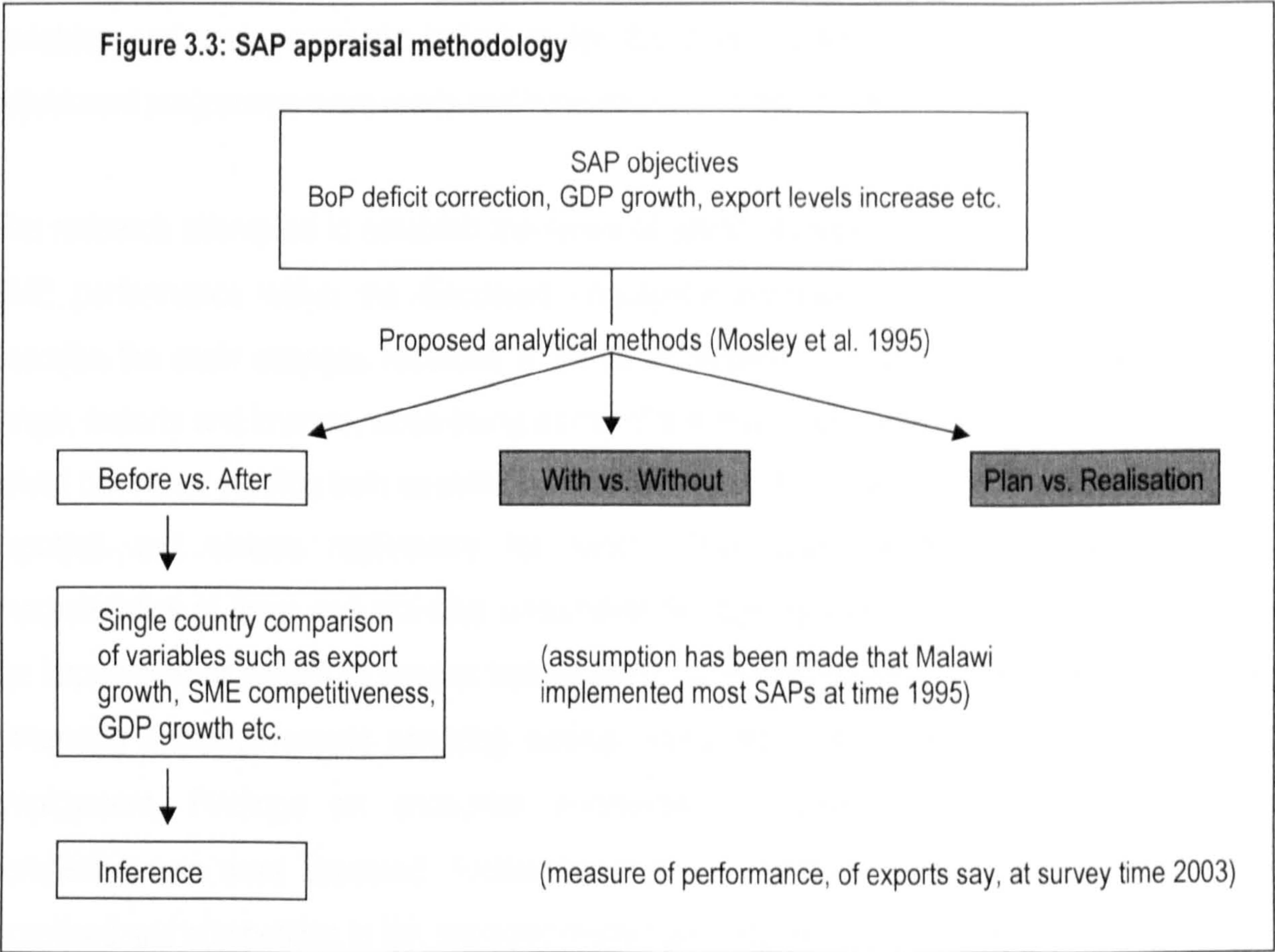
The first approach does not adequately differentiate the impact of non-adjustment factors such as terms of trade from the influence of adjustment. The second approach suffers from the same weakness as well as the complexity of determining which countries fits in with which category since many countries have implemented some adjustment policies but not others. The third approach overcomes the first problem but not the second (Stein 1999: 9).

Stein further argues that although the 'decomposition' approach factors out impacts of non-adjustment variables, it does not sort out relative merit of individual policies within the package. He argues that the 'with and without' approach utilises static social accounting frameworks for parameter determination and causes problems when moving from simulations to populations being modelled. Elsewhere, Mosley et al. described three 'yardsticks' that are available for assessing impact of the Bank's policies: plan versus realisation; with versus without; and before versus after (Mosley et al. 1995). They argue that the relationship between plan and realisation tells us very little about the impact of the Bank's programme as there may be other reasons for outcome of the targeted performance. They also argue that the before and after method is no better either, as differences in performance may once again be due to any number of extraneous influences such as oil crises, changes in world prices, serious drought, and so on, which are nothing to do with the variables under analysis. Mosley et al. point out that the 'before and after' method can show what happened but not necessarily answer why. As for the 'with' and 'without' method, they argue that it affords hope of separating out influences of programme from that of extraneous variables, but there has to be two countries which are identical in all aspects except for the fact that one is a programme and the other is a non-programme country. It has been argued that a number of studies carried out using these methods have presented rather contradictory evidence of the effects of adjustment (Mosley and Weeks 1993).

However, since this study examines effects of globalisation and adjustment on a particular country as opposed to comparison between countries, the method which affords time, resources, scale and achievement of the objectives of this research is the 'before and after' method. The choice of this method is supported by Goldstein (1986) who pointed out that the method is useful to show what happened within programme countries. The appraisal methodology of the 'before versus after' path,



presented in Figure 3.3, which is a slight modification of the model recommended by Mosley was followed (Mosley et al. 1995).



It should be noted that even though the SAPs were first implemented in 1981 in Malawi, most individuals were not aware of them then and hence had not made use of the advantages that the free trade policy provides until the political changes of 1995. This is the reason why, in this appraisal methodology, the assumption has been made that Malawi was fully complacent with most SAPs, including trade liberalisation, by 1995. However, 1981 has been used as the dividing and analysis point of the ‘before’ and ‘after’ periods of SAPs as implementation of these policies actually started in 1981 in Malawi.

The measurement and analysis of the impact of SAPs was based on the information and opinions gathered from entrepreneurs themselves through relaying what they have observed either over the years after 1981 or over the years after 1995. It did not matter very much whether the opinions referred to period after 1981 or 1995 as not all the SAPs were implemented, in Malawi, in 1981 anyway or soon after that. They have been gradual over the years and some of the reforms, like privatisation, had not been completed till recently. The aim was to get information on ‘what’ the



entrepreneurs observed as changes, in their opinions, and then draw inferences later on as to 'why', which could be because of the SAPs themselves or the implementation process itself, or some other factors over the years. And in any case the 'why' question is more complex than any of the three appraisal methods described. The comparisons of macro-economic performance variables and socio-economic indicators for the period before and after (pre and post 1981) adjustment programme were made and have been presented in Chapter Four.

The research attempted to establish the range of opinions/views regarding SAPs, globalisation and SME performance within the discussed conceptual framework. Entrepreneurs were asked to describe the main changes recorded in terms of production, employment, investments, product range, exports and imports, since being aware of the 'free trade' policy. The empirical investigation asked questions yielding both quantitative and qualitative data, such as on the proportion of output exported and various motivations for export. Data was therefore obtained on particular characteristics of firms and activities undertaken by them (yielding nominal or category data), on the importance or impact of various factors (such as the importance of inter-firm collaboration for enhancing competitiveness) providing ordinal measures, and on firm performance in terms of employment. Findings on enterprise involvement in international trade and sources of competitiveness were assessed. Production changes and technological upgrading were closely examined and competition in the domestic market and inter-firm linkages were analysed.

The researcher took the development of international competitiveness to mean moving towards the ability to sell in export markets without subsidy and to meet import competition without protection. 'Export' is an important factor as empirical analyses have consistently shown close links between economic growth and export growth (Fosu 1990, 1996). In the current economic era, if Malawi is to grow, it must not only diversify its exports into other areas but must also make progress in manufacturing. The survey probed competitiveness on the export side through questions about the export propensities of firms and whether exports account for an increasing share of output. In addition, responses were sought on the significance of the differing impacts of trade liberalisation. Due regard was particularly paid to the purpose of the survey, the accuracy required in the results, the cost, time and labour involved, and other practical considerations. Since funds and time were invariably limited, the aim throughout was to utilise them to best advantage. And as mentioned before, the field work was carried in two phases:



### ***The first phase: fact finding***

During this phase of the investigation, information was collected by means of informal in-depth interviews with key government and NGO officials in August 2002 (selection procedure for the participants is discussed in section 3.4.2). No structured questionnaire was used for these discussions and this helped to establish a relatively comprehensive body of perspectives. Outcomes and findings, which arose from these interviews, determined the research focus and design for the enterprise survey which followed in the second phase. The interviews were carried out with people in leading positions responsible for economic and SME sector development in government and non-governmental organisations in Malawi. Four government ministries and three non-governmental organisations (NGOs) were visited (see Appendix 3 for list and brief description of activities for each of them). The participants were mainly economic planners, policy makers and SME advocates. This phase had two main goals to achieve: firstly, to gain insight into the impact of globalisation and trade liberalisation on the SME sector (fact finding) as perceived by different actors other than the entrepreneurs themselves and to find out what strategies the Malawi Government and NGOs had put in place in order to develop the sector; and secondly for the findings to aid in deciding key issues to focus on during the second phase of the study.

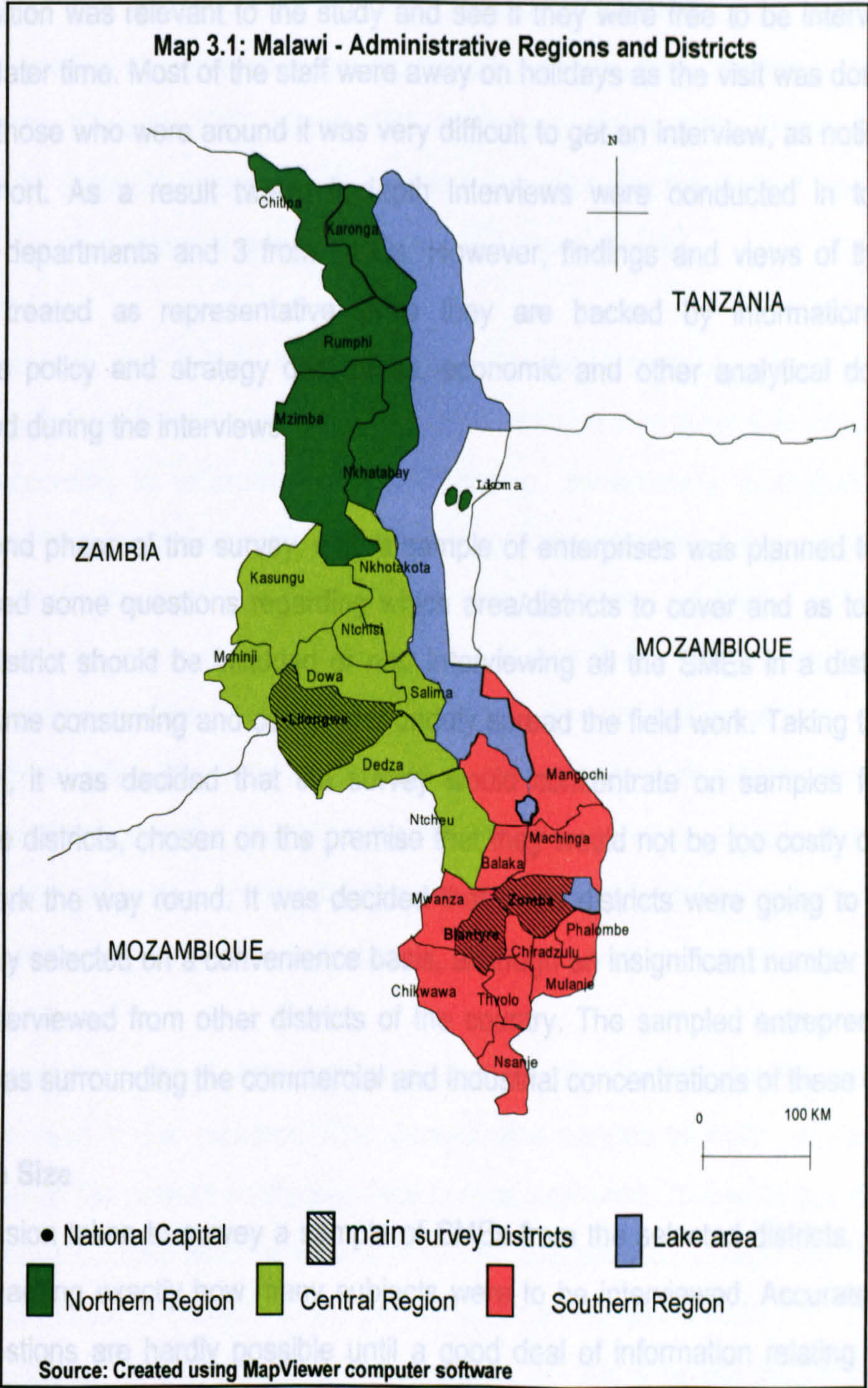
### ***The second phase: enterprise survey***

The enterprise survey was conducted over a four-month period from September to December 2003 and covered both informal and formal small and micro scale enterprises, operating in the most representative sub-sectors of activities in Malawi. A questionnaire was used for face-to-face interviews with entrepreneurs and a research assistant (RA) was hired to conduct the interviews. The discussion regarding the issues and implications of using an RA to carry out the interviews is presented in section 3.5.1.2.

## **3.4. Survey Coverage**

One of the methodological considerations of surveys is regarding whom to collect information from. The first step was to define the population to be covered. In this research, the population refers to all (both formal and informal) small and micro-sized enterprises in Malawi from which a sample was drawn. Malawi is divided into three administrative regions: North, Central and South which are further sub-divided into 27 districts (Map 3.1). There are four major urban centres in which reside about 13% of the population: Lilongwe, Blantyre, Zomba and Mzuzu city in Mzimba district.





Only a few individuals were interviewed during the first phase of the study and they were based in the two administrative districts of Lilongwe and Blantyre. These districts were mainly selected for reasons that they are where headquarters for most government and non-governmental offices are located and where most key officers are based, and this was also very convenient for the researcher. It was easier and time-effective to concentrate on one geographical area where one could easily move from one office/building to the other without having to travel long distances for the next interview.

The number of interviews covered was not pre-determined as it was difficult to make any contacts beforehand. It was a case of finding who was responsible for what and deciding which staff



member position was relevant to the study and see if they were free to be interviewed there and then or at a later time. Most of the staff were away on holidays as the visit was done in August and for some of those who were around it was very difficult to get an interview, as notice given to them was very short. As a result twelve in-depth interviews were conducted in total: 9 from the government departments and 3 from NGOs. However, findings and views of those interviewed have been treated as representative since they are backed by information gathered from government's policy and strategy documents, economic and other analytical documents, which were obtained during the interviews.

For the second phase of the survey, only a sample of enterprises was planned to be interviewed and this raised some questions regarding which area/districts to cover and as to whether certain areas in a district should be included or not. Interviewing all the SMEs in a district or area was going to be time consuming and costly, and unduly spread the field work. Taking these factors into consideration, it was decided that the survey would concentrate on samples from one or two administrative districts, chosen on the premise that they would not be too costly or geographically difficult to work the way round. It was decided that these districts were going to be Blantyre and Zomba, purely selected on a convenience basis, although an insignificant number of entrepreneurs were also interviewed from other districts of the country. The sampled entrepreneurs were fairly spread in areas surrounding the commercial and industrial concentrations of these districts.

### **3.4.1 Sample Size**

With the decision taken to survey a sample of SMEs from the selected districts, the question still remained regarding exactly how many subjects were to be interviewed. Accurate answers to the research questions are hardly possible until a good deal of information relating to the survey is provided. According to Moser and Kalton (1971), a sample needs to be of an adequate size for it to be representative of the population and if generalisations are to be made from survey findings. The number of subjects in the investigation depended on a number of factors connected with the research and which needed to be borne in mind and weighted up by the researcher in the process of reaching a decision about the necessary size of the sample. Most research literature (Alasuutari 1995, Becker 1998, Mason 2002) note accuracy of results, number of sub-divisions within the sample, response rate and resources available as the main factors to take into consideration when deciding sample size.

Firstly, due to an element of 'luck' in terms of who gets included in the sample, any sample might produce results which are different from the 'true' results of the population. In order to achieve



greater accuracy one might need to increase sample size and there are statistical procedures which can be used to calculate what specific sample size would be necessary to achieve a given level of accuracy (Cicourel 1967, Marsh 1982, Moser and Kalton 1971, Weber 1949). This factor was not used for determining sample size on the assumption that the method would have come up with a larger size than time and money available would have allowed.

Secondly, a sample may initially look quite large but might produce only very small returns in relation to specific sub-divisions. In this study, initial intention was to be able to subdivide sampled enterprises according to enterprise type like tailoring, construction, food-processing, furniture-making, basket weaving and according to entrepreneur characteristics such as age, sex, education, employment, business training and so on. A cross-tabulation of these variables meant five enterprise factors by five personal factors resulting in twenty-five subdivisions of the data. For a small sample size this means few cases in each sub-division and some cells ending up empty which is hardly an adequate basis for making generalisations. A big sample size was needed to ensure that subdivisions in the analysis were adequately catered for. Initially, the problem of subdivisions was planned to be overcome by a selection procedure called quota sampling, described in section 3.4.2, but in the end it was decided that this process was going to take longer and be costly.

Thirdly, the number of original sample may not equal number of responses that are finally obtained which can be used in the research. The sample size needed to have an allowance for non-responses even in the case of conducting face-to-face interviews. And lastly the size needed to be tailored to meet the constraints of time and money available for it. Basically, if cost and other practical limitations did not enter into the picture, there would be no basic difficulty in determining sample size required for achieving a given precision, but this simplicity disappeared with money and time limitations. The issue of response rate was not very crucial to calculation of the sample size, since a decision had been made to take a 'snowballing' approach to entrepreneur selection until the required number of units was achieved.

Initially, the survey interviews were planned to be carried out face-to-face by the researcher. This was thought of as a good approach for probing further and for clarifying any issues or concerns which entrepreneurs would have. It was worked out that maximum number of weeks that could be taken off full-time employment, by the researcher, was three. Thus sample size was determined by three practical considerations and assumptions: interviews would be carried out by the researcher herself, hence only one interviewer would be available; fieldwork would be covered over a three



week period such that interviews would be completed over that time span; and it was estimated that about 45-50 interviews would be conducted per week.

A combination of these factors suggested an aim of about 135 interviews in total within the given time limit. It was then decided that the planned sample size would be of the order 135 to 175 entrepreneurs determined mainly by the number of interviewers and how many interviews could be managed in the time at the interviewer's disposal. Unfortunately, the researcher was not able to go out herself for the field work in the second phase of the investigation due to financial constraints, as the research was self-funded. It worked out to be more economical to employ an RA, who was already experienced in face-to-face interviews, had previously undergone social survey training through the Malawi Centre for Social Research and was already based in Malawi. However, a decision was made to keep the sample size to the same range of between 135 and 175 as it was without doubt that this sample size would ensure that all aspects of relevance to the research questions would be covered. This decision is supported by an argument by Descombe that:

The use of surveys in social research does not necessarily have to involve samples of 1,000 or 2,000 people...Whatever the theoretical issues, the simple fact is that surveys ... are frequently used in small-scale research involving between 30 and 250 cases (Descombe 1998:24).

Descombe reckons that as long as a sample is made up of more than 30 people or events, it is adequate in social research. On that basis, achieving a sample size of 135 interviews was going to give good results. In the end a total of 147 entrepreneur interviews were achieved, which is within the original desired range given the financial constraints. There were 71 entrepreneurs sampled from Blantyre, 62 from Zomba and the rest were spread among a few other districts.

### **3.4.2 Sample Design and Selection Procedure**

One way of increasing precision of a random sample is to increase its size. Although, an increase in sample size will increase precision of the sample results, it will not eliminate or reduce any bias in the selection procedure (Clarke and Cooke 2004, Harper 1966). Stratification is merely a way of dividing the population into a number of sub-groups and allocating the sample between these sub-populations referred to as *strata*. Stratification does not imply any departure from the principle of randomness as a random sample is selected within each stratum. A simple random sample would provide unbiased estimates of measurable precision, but it could almost certainly be bettered through stratification by ensuring that special groups, locations, industry are correctly represented in the sample.



### 3.4.2.1 Sampling Theory

The idea of sampling is neither new nor unfamiliar in everyday life and the major advantage of sampling, as against complete coverage, is savings on money. This section explains in fairly general terms the principles underlying sampling theory. One of the objectives of a sample survey is to generally estimate certain population parameters. A sample is selected, the relevant statistic is calculated, and this statistic is used as an estimate of the desired population parameter. As statements based on sample results are always probability statements, a decision to cover only a sample, rather than every member of a population means leaving the field of description and certainty and entering that of inference and probability (Moser and Kalton 1971). Knowledge of some of the population members would be lacking and any conclusion about the population must be given in terms of probability. If worthwhile conclusions relating to the whole population are to be made from the sample it is essential to ensure that the sample is free from *bias*, and the problem of bias can be solved by taking a *random sample*. A random sample is a sample selected in such a way that every item in the population has an equal chance of being included. There are various methods of obtaining a random sample described in research and statistics literature (Clarke and Cooke 2004, Denscombe 1998, Murphy 1967), but they all depend on the selection being wholly determined by chance. Probably the best method of random selection is to number all the items and then allow a computer to throw out a series of random numbers which will identify the items to be used in the sample.

Occasions often arise when the selection of a pure random sample is not feasible. The obstacles arise when such a sample would entail much expensive travelling for the interviewers, when 'hunting out' the people selected would be a long and uneconomical task and when all the items in the population are not known. However, as pointed out in many research literatures, great care has to be taken to ensure that a sample population is truly representative (Clarke and Cooke 2004, Harper 1966, Moser and Kalton 1971). In very large surveys, statistical sampling techniques are employed in order to produce a sample, which is as far as possible, representative of the population as a whole and generalisations are then made from the findings. In small studies like this one, one can only do the best they can with as much as time and money allows. As Bell argued:

All researchers are dependent on the goodwill and availability of subjects, and it will probably be difficult for an individual researcher working on a small-scale project to achieve a true random sample. If that proves to be the case, you may be forced to interview anyone from the total population who is available and willing at the time (Bell, 1999:126).



Such was the case during the first phase of the survey as there was no sampling frame from which a random sample could be selected. In addition, the researcher had questions in mind which individuals in only certain work positions could provide answers for and hence the subjects interviewed were obtained by a method, which does not embody the feature of randomness, known as *purposive sampling*. Purposive sampling is a method of sampling whereby samples are selected on the grounds of convenience and accessibility. This method is described by Denzin and Lincoln (2000) as a method whereby researcher seeks out groups, settings and individuals being studied from where they are most likely to be found. Denzin and Lincoln also pointed out that many social researchers employ purposive, and not random sampling methods as it is more convenient. And as noted earlier on, for this study it was a matter of interviewing whoever was available and willing at the time. With regards to the second phase of the survey, a combination of sampling techniques was used due to time and financial limitations.

In order to overcome the constraints, which make random sampling impossible, Harper (1966) suggested some ways of the sampling process such as *multi-stage* and *cluster sampling*. In a multi-stage sampling technique the country, say, is divided into a number of areas, and required number of coverage areas are selected by random means. A random sample of the target population within each of these areas is then interviewed. Although the technique means the interviewer has to travel to different parts of the country, once in an appropriate area interviews can be carried out with virtually no further travelling and this brings the cost of the survey within reasonable bounds. Cluster sampling is used when it is the only way a sample can be found and in cluster sampling, the country is divided up into small areas, much as with the multi-stage method. It is advantageous to be able to confine the special listing to an area or group. Interviewer then visits the areas to interview every person they can find that fits the definition given (entrepreneur with micro or small size business, in this case). Cluster sampling technique was applied in the second phase of the survey as it was more time and cost effective than random sampling. Had all units of enquiry, both formal and informal entrepreneurs, been listed on a convenient register (sampling frame), one way of sampling would have been to pick a random sample from the entire list. However, this would have spread the sample all over the whole districts with consequent high fieldwork costs and much inconvenience.

#### **3.4.2.2 Sample Selection**

After selecting the survey districts the next stage was selection of entrepreneurs to be interviewed from the selected areas/clusters. The aim was to visit naturally occurring clusters of enterprises and by focusing on these clusters, it was thought that it would save a great deal of time and money on



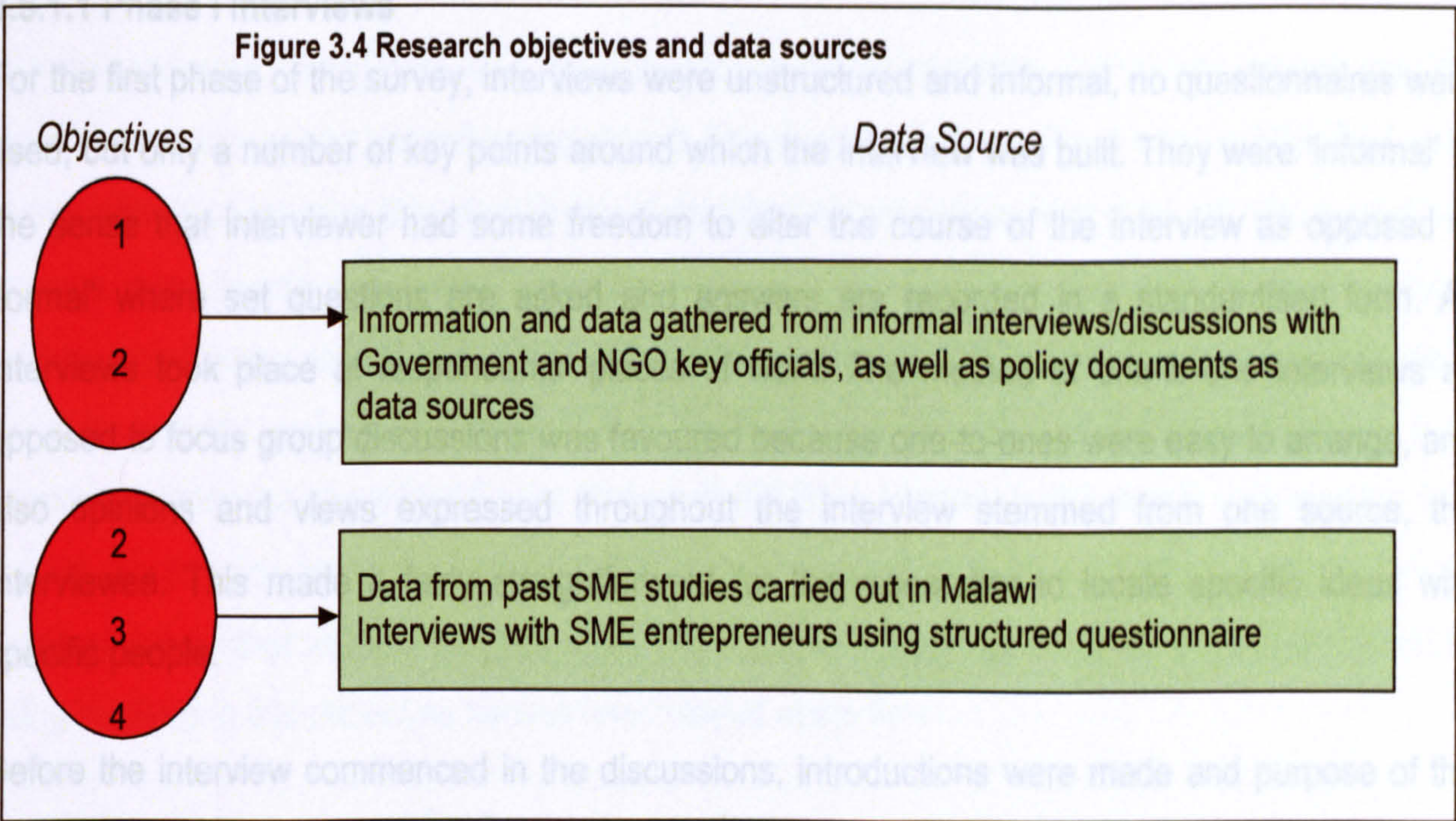
travelling to and from visiting enterprises scattered throughout the length and breadth of the land. However, it was very difficult to find concentrations (clusters) of enterprises as most of them operate from home hence appropriate method was to ask people in an area if they knew anybody running a business and see if they were available to be interviewed. This is the approach referred to as *snowballing* by Denscombe (1998), and it was the selection procedure used for picking entrepreneurs. With this method each individual interviewed was asked to name other people who they thought would be relevant to be interviewed for the purposes of the research. The sample thus snowballed in size until the minimum number of 135 entrepreneurs was reached, and thereafter until resources were exhausted. This approach has been argued for by some writers in that 'our time and access for fieldwork are almost always limited. If we can, we need to pick cases which are easy to get to and hospitable to our enquiry' (Stake 1995:4).

### **3.5 Data Collection Methods**

The study design was directed towards achieving the research objectives with required accuracy and within given resources. The subject matter, the unit of enquiry and the scale of the survey govern the choice of data collection method. For an educated section of a population, like professional groups, a mail questionnaire might be adequate but for general population entailing many complicated questions would call for personal interviewing which might vary from the standardised, formal technique down to informal conversations. In social surveys, the main methods of data collection are observation, mail questionnaire and personal interviews. Surveys also generally make some use of documentary information, thus, statistical data, documents and historical records. The main data collection methods for this study were personal interviews and documentary sources, governed by the fact that most small enterprises are not registered and the mail address system is not well developed (Malawi National GEMINI 2000).

Figure 3.4 is a presentation of data sources from which answers to the research questions were obtained. A combination of different sources of data collection methods were used in an effort to measure quantifiable aspects as well as less easily measured aspects. These included informal in-depth interviews, structured interviews and documentary sources of data. Criteria for measuring the economic development and growth of a country are mostly dependent upon the traditional macroeconomic models and their indicators, and as such the main sources of data were the National Statistical Office, National Economic Council and Ministry of Commerce and Industry and WB indicators. Macro-economic indicators in two fields of socio-economic and monetary-fiscal measures are very useful in tracking trends of the country over time.





Before going into the field, the necessary books and journal literature, past investigations of relevant official reports and statistics were consulted. Findings from these sources have been presented in Chapters Two, Four and Five. The literature reviewed, made aware of available existing work already undertaken in this area of research and this helped to identify key issues, crucial questions and obvious gaps in the current state of knowledge in the research topic. The aim was to avoid repeating research that had already been conducted and to provide a foundation on which to build new research.

The information from the different types of documents supplemented data, which was obtained through interviews. It is possible that answers to some of the questions the survey intended to cover could be obtained from the available information, but then documentary answers provide a check on the accuracy of survey results. It was necessary to carry out a survey since past investigations, conducted for entirely different purposes from this one, did not suit this research's purposes. Moreover, the full data set from previous studies is not generally available to an outside researcher anyway.

**3.5.1 Interviews**

As said, personal interviewing was the main data collection method for this study. The researcher carried out the interviews/discussions with the government and NGO officials during phase I and an RA conducted interviews with the entrepreneurs in the survey phase II.



### 3.5.1.1 Phase I Interviews

For the first phase of the survey, interviews were unstructured and informal, no questionnaires were used, but only a number of key points around which the interview was built. They were 'informal' in the sense that interviewer had some freedom to alter the course of the interview as opposed to 'formal' where set questions are asked and answers are recorded in a standardised form. All interviews took place at respondents' places of work. The method of one-to-one interviews as opposed to focus group discussions was favoured because one-to-ones were easy to arrange, and also opinions and views expressed throughout the interview stemmed from one source, the interviewee. This made it fairly straightforward for the researcher to locate specific ideas with specific people.

Before the interview commenced in the discussions, introductions were made and purpose of the research was explained to the respondent (Appendix 2). It was also explained that any views or findings, discussed with individuals, would be presented anonymously, such that they could not be traced back to interviewees. All conversation was carried out in English, the official language for the country. A copy detailing study objectives and Conceptual Framework (Figure 1.1) was also presented to the respondent. After the introductions, verbal consent was asked from the individuals to commence with the interview and requested if it was acceptable to tape-record the conversation. Unfortunately all but one interviewee did not want to be tape-recorded such that note-taking was the only mode acceptable to all for gathering their views.

Themes of the research were introduced to start off the discussion and then letting the interviewees develop their ideas and pursue their train of thoughts. Emphasis was placed on interviewee's thoughts and allowing them to 'speak their minds' was a better way of discovering things about complex issues. The informants were encouraged to talk about the subject matters under research and there was no pre-determined framework for recording answers or views (Appendix 4 for one of the interview transcripts). The researcher confined to elucidating doubtful points, to rephrasing the respondent's opinions and to probing generally. Different items of information were obtained from the different respondents, which made it a bit harder to compare and aggregate the results later on during data analysis. At the end of each interview, interviewees provided copies of documents, which they felt would be relevant to the study (full list of the documents is given in Appendix 6). And as pointed out, information from these documents provided a check on the accuracy of the survey and perspectives obtained from the interviews. The documents also formed a statistical background against which the significance of the survey results would be judged.



### 3.5.1.2 Phase II Interviews

A male assistant, competent and experienced in social research interviews carried out the entrepreneur survey and worked unsupervised. The decision to hire a RA to carry out the field work of the second phase was based on financial and time constraints as it worked out less expensive, to pay somebody who was already in Malawi, with years of experience, fully comprehends the local language and understood the local culture, rather than to fly out there myself as I was self-funded. He was selected mainly on the basis that he had previously carried out several similar type interviews under the Centre for Social Research (CSR) in Malawi. In this way it was assured that the RA would understand the nature of this type of work and would not distract participants into areas of inquiry that were of no relevance. The RA was grateful for the money and experience of being involved in this project as he was unemployed at the time.

The RA was given adequate briefing (during the first phase visit) about the purpose of the research and an opportunity was given to discuss ethical considerations and consent as well as to discuss the questions. No doubt this may pose some questions regarding the quality and reliability of the data given that the RA only had a partial understanding of my requirements. On the other hand, it could be argued that, absence of complete knowledge may have created impartiality. Anyhow, the RA had received formal training, in gathering social data, from the CSR. He was thoroughly briefed on issues regarding data quality management, what sort of follow-up and supplementary questions to ask and there were telephone conversations and discussions throughout the survey period between the researcher and RA. The survey was carried out over a four months period and completed questionnaires were being mailed in batches from Malawi which made it easier to constantly monitor the process and responses and communicate feedback to the RA when needed. In addition the questionnaires were structured and already translated into the local language ready for use by the RA. This process ensured that the quality of the collected data was enhanced.

There are both disadvantages and advantages to using an RA to carry out field work on behalf of the researcher. It is possible that the RA could have brought their own views, on the subject, to the interview and presented the interview questions in such a way that was leading to the respondents. It should also be appreciated that the RA himself is only human and there is nothing stopping them from being subjective and influencing the responses from the entrepreneurs. Or it could also be that the RA himself misunderstood the questions and meanings of other words, though in local language, and hence obtain responses which were not pertaining to the questions. Furthermore some responses could have been better probed had the researcher carried out the work herself. Another disadvantage for placing all the interview responsibility on the RA is that if she/he is not a



trustworthy individual they could end up completing the interview questionnaires themselves, which would invalidate the survey results. Whilst acknowledging these issues, it should be emphasised that the researcher had all the confidence in the RA and there was no doubt that he had the necessary skills, integrity and ability and experience to carry out the interview work on her behalf, and above all trust was placed on him as much as trust could have been equally placed on the researcher had she conducted the interviews herself.

The main benefit to be gained from using a RA is that no emotions on the part of the researcher play any role during the interviews (Ellen 1984). Sidaway (1992) argued that regardless of whether one is local or not, the unequal relation between researcher and researched often remains. Unequal power between the researched and me could, possibly, have had some negative consequences for the fieldwork. Respondents could have told the researcher what they believed she wanted to hear or equally the researcher could have probed them to tell her what she wanted to hear, influence responses in some ways. The data collected not only depended on what the informants were willing to reveal, but also the appraisal of, and the trust they placed in the RA. However, carrying out the survey oneself obviously adds depth and colour to the data collected. Without doubt, if finance and time were not constraints, it would have been more advantageous for the researcher to carry out the interviews herself.

Before the interviews commenced, sufficient background information was provided to respondents about the research, thus they were informed of the purpose of the research, how information gathered would be used and that the interview was voluntary hence they were not obliged to respond to any questions that they did not feel comfortable with (see Questionnaire in Appendix 7 for exact wording). Gratitude was expressed at the end of an interview to all participants.

When work is finalised, a summarised report of the thesis is to be made available to the people and institutions which supported this work. However, for the entrepreneurs, there is the issue of a restriction to access to the report because only those who can read English would be able to read the report. Plans are in place to produce a summarised report of the results, in the local language, same way as the questionnaire was translated, for the benefit of the entrepreneurs. It is hoped that they will benefit, in the long-term, from policy changes which may be brought about as a result of this research.



### 3.5.2 Questionnaire Design

Most social surveys use a questionnaire of some kind, and the framing and arrangement of questions is perhaps the most substantial planning work. Using a standard questionnaire in the entrepreneur survey was opted for because it is a good way of collecting certain types of information quickly and relatively cheaply as opposed to in-depth interviews, which require more time. It has also been said that a study can be more reliable if similar results are obtained using the same questions and asked in the same way (Gilbert 2001). After deciding on exactly what information was needed to be collected from the entrepreneurs, it had to be ensured that a well designed questionnaire was produced that would give the information needed, be acceptable to the subjects and that would give no problems at analysis and interpretation stage (Descombe 1998). The Conceptual Framework and the research objectives guided the design of the questionnaire. After several attempts at wording in order to remove ambiguity and to ensure that subjects would understand exactly what was being asked and also to ensure that the researcher would be able to classify and analyse responses without too much difficulty, the questionnaire was produced (Appendix 7).

Smith (1975) argued that questionnaire wording is a significant factor in survey research and suggests that there must be a shared vocabulary between researcher and respondent. For example in this study, there were concerns over whether the respondents would understand or how they would interpret the conceptual words of 'globalisation' and 'structure adjustment'. It had to be made sure that both researcher and entrepreneurs had the same understanding and interpretation of the words otherwise the results would be distorted if they meant different things to different people. Thus, in order to minimise the problem of misjudgement of the impact of 'SAP' and 'globalisation' by the respondents, these words were not presented straight, as they stand. Their definitions, instead, were turned into questions and this was first pilot-tested on a group similar to the one that formed the population of the study in order to gauge what the understanding was and if required make the necessary adjustments to the wording to ensure that the results would not be far off from meanings and definitions in the literature. Not many locals would know the meaning of globalisation or structural adjustment hence the need to word the questions in such a way that they were simple and straight forward and at the same time be in the context of the definitions of the concepts in the study. The questionnaire was also pilot-tested to check that all questions and instructions were clear and to enable researcher to remove any items, which did not yield usable data. The pilot was carried out through mailing out the questionnaire to the RA in Malawi who conducted the test interviews on a few individuals whom he could find and who were willing to



participate. The responses enabled the researcher to revise the questionnaire for use in the main survey.

Information was gathered on characteristics of owners and enterprises, operating environment, impact of structural adjustment measures, enterprise operations and how entrepreneurs responded to the measures. The questionnaire included both open and pre-coded questions in order to give respondents freedom to decide on aspect, form and detail of their answers and also give them a listed number of answers from which to choose. In some cases researcher had not been able to reasonably determine in advance what the main categories would be such that it was best to have open questions to which answers were coded later on once the range and distribution of answers became clear. And also, inclusion of open questions has its advantages in that information provided by the respondent is more likely to reflect the full richness and complexity of the views held by the respondents (Descombe 1998). Most questions were structured and had tick boxed for ease of analysis and some questions had been designed to give the respondents opportunity to give their own views on the topic being researched or to raise a grievance. The questionnaire was designed in English but another version was produced which translated the original version directly into local language for interview purposes.

### **3.6 Data Processing, Analysis and Interpretation**

Although fieldwork is the central stage of a survey, an enormous amount of work remains to be done after the raw data has been gathered. Soon after the fieldwork was completed, processing and analysis of the materials followed. Completed questionnaires were scrutinised for errors, omissions and ambiguous classifications before they were ready for coding and inputting onto a database. Analysis, usually involving calculation of statistics, followed after the database was completed. Data was processed on a Personal Computer using Statistical Package for the Social Sciences (SPSS) software to create tables and cross-tabs. Since the questionnaire had different types of questions which included listed, category, scale, grid, verbal/open and ranking questions, the responses required different ways in which to be analysed and presented. Some of the data collected using the questionnaire was quantitative hence unit of analysis were numbers whereas some of it had to be coded and quantified before analysis.

Information gathered during the first phase of the survey was qualitative and hence unit of analysis were words. The words had to be quantified and coded before analysis. As the aim of the in-depth interviews was to get a holistic perspective, variables were not isolated as views were seen 'in context'. Lincoln and Guba commented that qualitative research assumes that realities are wholes



which cannot be understood in isolation from their context and they cannot be fragmented for separate study of their parts (Lincoln and Guba 1985). Since conversations were recorded in note form, the material had to be transcribed by indexing responses with respect to theory underlying the research. All the responses were written onto a separate sheet and scanned in order to see whether there were any recurring themes. Issues were categorised into concepts of Globalisation, SAPs, Trade liberalisation, and Competition. Content analysis was necessary to deal with the material, and categories of common criteria were grouped together in the analysis. The analysed data was then reviewed in the light of research questions. Responses from the first phase of the study provided useful pointers to types of issues which were followed up in the SME interviews. And some of the responses provided useful quotations to illustrate certain points in the report.

For the second phase of the study the units of analysis were *entrepreneurs* and *enterprises*. After data analysis, findings were presented and interpreted. The results have been presented in tables, cross-tables and graphs in Chapter Six. Since the sample was selected in a non-random manner, any generalisations of results have been treated with caution.

### **3.7 Reflexivity, Reliability and Validity**

Reflexivity concerns the relationship between the researcher and the social world (Descombe 1998). It suggests that researcher cannot achieve an entirely objective position from which to study the world. The researcher acknowledges that one cannot stand outside the social world that she is studying and hence was aware of how she would be perceived as to what extent she had influence on the results. Explanation and description of how researcher gained access to informants and how research was explained to them is detailed in the above sections. The researcher takes the view that data is not just something 'out there' to be collected but as something created through a social process. The data was gathered through a social interaction between researcher/interviewer and informants so that the research itself is a creative process which researcher herself is part of. As noted before, the entrepreneur interviews were carried out by the research assistant, and it has been pointed out that sometimes using an 'outsider' might be better placed to hear a piece of information which to the researcher herself might be too mundane or too obvious to register as an important factor (Descombe 2003). The RA approached the entrepreneurs with a fresh mind/clean sheet without attached meanings to the concepts as would have the researcher, after carrying out a literature review on the concept. But then as said, the RA is also human and would not stand entirely outside the informants that he was interacting with. However, by using a standard questionnaire for all meant that interviews and responses were from the point of view of respondents and not from the RA's own way of seeing things.



The researcher was mindful of the importance of reliability and validity of measures and procedures. Readers and users of this research will be asking how accurate are the findings and representation of what actually exists and the extent to which the methods are really measuring what was intended to be measured. Reliability concerns the extent to which the survey would give consistent results if applied by different researchers more than once to the same people under standardised conditions. The questionnaire included a repetition of questions from previous similar studies so that comparisons could be made between studies over time. Validity of the research was assessed by looking at evidence, at how the research was carried out, whether anything could have interfered with the research process and confused the results, and the nature of the connection between the evidence and the generalisations. This was one of the reasons for adopting the pre-structured approach towards the respondents as this method has a high validity as it is standardised and controlled. However, this approach could be artificial since social interaction is more complex. Thus, it may produce results, which are high on internal validity (causal inference) but low on the external validity in terms of generalising to a wider population. Small-scale studies using in-depth interviews with a handful of informants may be low on internal validity but high on external validity because they relate to people in everyday settings. This was the case with the first phase of the survey where in depth interviews were carried out on a handful of individuals. With internal validity, the conclusions are correct within a particular investigation or within the context of a specific settings and this is more important in this study as the aim is not necessarily to generalise findings but make inferences.

### **3.8 Summary**

The choice of the research methodology was guided by the research aims, objectives and availability of resources. A positivist approach to the research was adopted whereby respondents were given the power and freedom to discuss and inform their views on SAPs and globalisation and how their businesses have been affected. The 'before' and 'after' SAP appraisal method was opted for as this afforded time, financial resources and scale of the project, furthermore the intention was to show what was happening within a particular country of study, Malawi. As a social research, three steps were followed in the study process. Firstly, the theoretical context was discussed from the literature, followed by the design of research methodology and survey methods, and lastly the actual collection of the data. Concepts were formed at the theory construction stage and from the data findings deductions were made.



Field work of the survey was carried out in two phases. The first phase involved in-depth interviews with a number of relevant key government and NGO officers (purposively selected) in Blantyre and Lilongwe districts, and this was carried out by the researcher herself. No structured schedule of questions was used and the discussions were guided by the conceptual framework in Figure 1.1. Note-taking was the main mode of recording the discussions. The information, which was qualitative, was later transcribed, quantified and coded before being analysed. The findings from this phase highlighted the issues to be taken into account in the design of the second phase questions.

The second phase of the survey work involved structured interviews with a sample of entrepreneurs of small enterprises in the country. The sample was drawn from two main districts of Zomba and Blantyre which were selected for ease of travel between interviews. The number and size of the entrepreneurs to be included in the sample was limited by availability of time and finances. The sample units were purposively selected through snowballing, by simply asking around for entrepreneurs who were available and who would be kind enough to want to be included in the study. The interviews were conducted by a well trained and qualified research assistant using a structured questionnaire which was pre-translated into the local language.

The key factors and concepts, presented in Chapter One, guided the research questions in the questionnaire design stage. In addition to questions on SAPs and globalisation, other factors such as educational levels, entrepreneur skills and training, inter-firm linkages, finance, market, and infrastructure, which also affect the performance of enterprises, were also included as questions for analysis. Respondents were asked to indicate changes over a period of time as observed and understood by themselves. Although the questionnaire included some open-ended questions, most of them were pre-coded and as such most of the data gathered from this phase was quantitative.

Data and information from official documents and statistical sources were used to complement and supplement the information and views gathered from the individuals. All the information and data were gathered as evidence for the analysis of the Malawi SMEs in the context of SAPs and globalisation. The researcher is confident of the reliability and validity of the results, and that the objectives set out were achieved through the discussed methods and tools.



## **Chapter Four**

### **Malawi, Historical and Economic Developments**

#### **4.1 Introduction**

This chapter discusses the Malawi economy and economic policy in light of the challenges posed by SAPs and globalisation. Globalisation has significant implications for Malawi, a landlocked country in the south-east of Africa, far from the centres of world capital. Dramatic changes in the international context since the 1970s and global processes have been affecting the Malawi domestic policy and domestic deregulation in Malawi has profoundly altered the domestic economic context within which the country operates. Globalisation is therefore used as a tool to examine the context of Malawi's domestic economic policies and how it has been affecting the economy and economic activities.

The chapter is organised as follows: the second section introduces Malawi, and information is provided about the physical geography of the country, major historical developments and social-economic issues; the third section presents detailed information about economic policies and performance since independence up to the period of economic crisis; section four discusses the Malawi political and economic reforms of the 1980s, highlighting major policy developments in the agricultural and industrial sectors; on the impact of the reform measures on the Malawi economy is presented in section five; section six provides an update on policies and the Malawi economy in the 2000s; section seven summarises the chapter.

#### **4.2. Geographical description, Historical background and Socio-economic characteristics**

This section provides a historical background to Malawi and sets the background context in order to understand why Malawi is what it is today and where the country is coming from in terms of its economic make-up. Geographical location, political history and population characteristics presented in the following sub-sections.

##### **4.2.1 Geography and Historical background**

Malawi is situated in the south-east of Africa (Map 1.1) and stretches over a total area of 118,484 sq. km of which 20% is covered by Lake Malawi and other smaller lakes (Moyo et al. 1993). The country is landlocked and bordered by three other countries: Tanzania in the north, Zambia on the western side and Mozambique in the south-east.



In 1891 Malawi (then Nyasaland) became a British protectorate under Africa's colonisation. The Nyasaland protectorate was not a profitable asset for the British as the area was unsuitable for agricultural practices of Europeans, and less than 500 British farmers lived in the protectorate at any one time (Pryor 1990, Quinn 1994). These settlers mainly lived in the southern region of the country where they grew tobacco and tea on large plantations. During the colonial period, the central region was characterised by African smallholder agriculture while the northern region was heavily dependent on remittances from people working in the mines in South Africa (Africa Watch 1991). In order to strengthen the economic position of the colony, in 1954 a federation with Northern Rhodesia (now Zambia) and Southern Rhodesia (now Zimbabwe) came into effect. The African population was strongly opposed to this federation because of the racist practices in Southern Rhodesia and because they feared that possible economic gains would only benefit the British settlers.

In 1958 the struggle for independence started in Malawi. The first national elections were held in 1961 and were won by the Malawi Congress Party (MCP). In 1963 the federation of Rhodesia and Nyasaland was dissolved. On 6 July 1964 Malawi became an independent state under the leadership of Kamuzu Banda. In 1966 Malawi became a one-party state. At the end of the British colonial period, Malawi was left with a dualistic agricultural economy under which large expatriate-managed estates produced tea, tobacco and cotton for export, while local smallholder farmers produced subsistence maize. A small commercial and industrial centre in the southern region had been established, which included cement, bottling, tobacco processing and transport related activities. The country had no substantial mineral resources and its main assets were moderately fertile soils, good water resources and a climate favourable for crop production. There was no direct access to the sea, capital, technology, skilled labour and managerial capability.

In March 1992 Banda's regime was faced with an unprecedented form of criticism from within the country and with pressure from various Pressure Groups, Banda finally agreed to a referendum in October 1992 on the issue of multi-party system of government. The referendum took place in June 1993 and a majority of people voted for multi-party variant (van Donge 1995). Parliamentary and presidential elections were held in May 1994 and were won by United Democratic Front (UDF) party, which was the ruling party at the time of writing of this report.



#### **4.2.2 Population distribution and growth**

In 2005 the population of Malawi was estimated at around 12.9 million with a population growth rate of 2.2% per annum (WDI 2006b). The southern region where Blantyre, the country's commercial and industrial city is located has 50% of the population. Lilongwe is the capital city and it lies in the central region. The northern region, with 11% of the population, is the poorest and least developed of the country's geographical regions. According to the World Development Indicators, 83% of the population resided in rural Malawi in 2005, although urbanisation was growing rapidly at an average rate of 5.7% per annum between 1990 and 2005 (WDI 2006b). It has been reported that the population density of Malawi in 1964 was four times higher than the average figure for all African countries (Hooker 1970). The population density nearly tripled during the following decades from 38 in 1970 to 109 in 2005 and was three times higher than that for SSA average of 32 persons per sq km in 2005 (WDI 2006b).

Since the 1970s nearly half of the population of Malawi has always been under 15 years of age (Table 4.1). In 2005 life expectancy at birth was relatively low at 40 years compared to 51 years for SSA average, and 36% of the adult population was illiterate. Infant Mortality Rate was still one of the highest in the world although it declined from 189 deaths per 1000 live births in 1970 to 110 in 2005 (Table 4.1). Malawi is one of SSA countries severely affected by the Human Immunodeficiency Virus (HIV) and Acquired Immune Deficiency Syndrome (AIDS) epidemic and it was reported that HIV/AIDS prevalence rate, amongst adults aged 15-49 years, rose significantly from 1.6% in 1987, when the first incidents were recorded to 12.2% in 1995 but stabilised close to 14% between 2000 and 2005, this being below the reported 20-30% southern African average (UNDP 2005b).

The IMF expressed concerns in the 1990s that as the country was moving into the 21<sup>st</sup> century there was no appreciable progress made on social indicators since independence in 1964 (IMF 1998). Today, Malawi still ranks amongst the poorest countries in the world with a Gross National Product (GNP) of US\$161 per capita in 2005, as compared to a GNP of US\$744 average for all sub-Saharan Africa countries. External debt was estimated at US\$3.42 billion in 2005, up from US\$1.56 billion in 1990 (Table 4.1). High population density, intermittent droughts, diseases, small land holdings, traditional agricultural techniques and pervasive poverty all contribute to deforestation, overworked soils and low agricultural output.



**Table 4.1: Malawi, Statistical Trends, 1970-2005**

	1970	1975	1980	1985	1990	1995	2000	2005
Population (million)	4.5	5.2	6.2	7.2	9.5	10.11	11.51	12.9
Population density (inhabitants per sq. km)	38	44	52	61	80	85	97	109
Average annual population growth rate (%)	2.7	3.2	3.1	4.4	3.8	1.4	2.5	2.2
Population structure (% of total population):								
population age-group 0-14	46.7	47.3	47.5	47.6	46.7	44.6	46.2	47.3
population age-group 15-64	51.0	50.5	50.2	50.0	50.7	52.3	50.9	49.7
ages 65 and over	2.3	2.2	2.3	2.4	2.6	3.1	2.9	3.0
Population distribution (% of total):								
rural population	94.0	92.3	90.9	89.7	88.4	86.7	84.9	82.8
urban population	6.0	7.7	9.1	10.3	11.6	13.3	15.1	17.2
Life expectancy (at birth)	40.8	41.8	44.9	46.0	45.7	43.1	40.4	40.2
HIV population prevalence (%) (population aged 15-49)	..	..	..	..	9.3	12.2	14.4	14.1
Infant Mortality Rate (per 1000 live births)	189	171	157	150	146	133	117	110
Adult literacy rate (% of ages 15 and above)	30	37	42	44	52	62	64	64
GNP per capita (US\$)	..	220	230	170	180	170	170	161
Total external debt (\$million)	..	122	821	988	1,558	2,140	2,239	3,418
Urban population growth (annual %)	6.5	7.7	6.2	6.8	7.0	6.0	5.1	4.8
Access to improved sanitation (% of urban population)	36	52	55	57	60	62	64	66
Forest area (% of total land area)	..	..	..	..	41.4	34.7	36.2	27.2

Source: World Bank, World Development Indicators, various years

.. = data not available

### 4.2.3 Environmental factors

Environmental degradation is a serious problem in Malawi as the population continues to grow and exert pressure on the limited resources. The population of Malawi was only 4 million in 1966 and today the estimate of 13 million people implies that it has more than tripled in less than 40 years. The country has moderate fertile arable land which covers only half of the country's land surface and must be cultivated with only one short rainy season per year. The pressure on land has increased such that there is an increase in the cultivation of marginal land, more fragile soils and steeper slopes. Forest area which was 41% in 1990 was reduced to 27% of total land area in 2005 with average annual deforestation of 0.9% compared to 0.6% for SSA between 1990 and 2005 (WDI 2006b). As more marginal land continues to be brought into cultivation, more soil erosion and declining productivity is being experienced.

The rainfall is seasonal and extremely variable, and the country has experienced severe drought in succeeding years in the 1990s. Use of fertilizer, inter-cropping strategies, use of hybrid seeds and other innovations are being adopted at a faster rate than expected. Some districts, particularly in



the southern region, have population density of over 400 persons per square kilometre in arable land areas, making Malawi one of the most heavily settled countries in Africa. In most parts of the southern region there has been massive deforestation such that fuel wood, which is the main source of energy, is in short supply. It has been argued that a combination of poor soils, use of marginal land, high population densities and an increase in the rate of forest destruction has exacerbated environmental pressure in the southern region of the country (Kalipeni 1996). With population pressure, the intensity of internal migration is growing and movement is generally towards the urban centres of Blantyre and Zomba in the southern region, and Lilongwe in the central region. Urbanisation has exceeded sanitary carrying capacity in these cities. With urbanisation growing at a fast rate, access to improved sanitation facilities only increased from 60% of urban population in 1990 to 66% in 2005 (WDI 2006b).

### **4.3 Post-independence Economic Trends and Policies**

This section discusses policies and economic trends since independence starting with the period of inward-oriented and import substitution policies through the WB policies of economic reform to the early 1990s when it was realised that the reform policies were not working and targets set out in the 1980s were not being met and there were unsatisfactory outcomes.

#### **4.3.1 The Malawi Economy before SAPs**

Following independence in 1964 Malawi's development strategy was aimed at achieving growth through estate-led agriculture, public investment in infrastructure, inward-looking oligopolistic industrial activity and self-sufficiency in food production. The economy was run through a complex relationship between the corporate, financial and parastatal sectors. At the centre of these interactions was the Press Holdings, a large, private holding company owned by the President with equity interests in virtually every sphere of the Malawi economy, including majority shareholdings in the country's two commercial banks. Other two important parastatals, Agricultural Development and Marketing Corporation (ADMARC) and the Malawi Development Corporation (MDC) also held shares in the banks. Press, with easy access to financial resources, borrowed heavily, domestically and abroad, often under Government guarantees (Mhone 1987). Growth strategy depended upon a high implicit taxation of the smallholder sector with surpluses used for investment in parastatals. While this caused the smallholder sector to stagnate, the parastatals became the engine of growth (Pryor 1990).

The Malawi economy itself was characterised by three main sectors: the colonial estate sector which produced 40% of the country's merchandise exports (mainly tea and tobacco); the



smallholder sector producing for subsistence, providing a marketed food surplus, and producing export crops amounting to 50% of merchandise exports; and a labour reserve sector which supplied estate labour and migrant labour to neighbouring countries. The economy was, and still is, predominantly agricultural, lacks mineral resources, capital and skilled labour and possesses a limited small domestic market (McCracken 1988). With regards to these constraints the post-independence development strategy focused on an export-oriented, agro-based and labour-intensive expansion path with import-substituting industrialisation playing only a secondary role and restricted to a narrow range of consumer goods which were already afforded a high degree of natural protection by the country's land-locked position.

In the country's first major post-independence strategy document, the Malawi government placed highest priority on the development of the agricultural sector via increased productivity, with a particular policy emphasis on improvements in the smallholder sector (Government of Malawi 1971). In order to support the expansion of export-oriented agriculture, the second highest priority was placed on the development of transport, communications, marketing infrastructure and other forms of necessary physical infrastructure. The development plan placed the manufacturing sector in a subsidiary role to agriculture and stressed the development of both import substituting and export-oriented industries. The focus was on: private investment, including foreign capital; labour intensity; and on the selective use of tariffs, rather than quantitative restrictions, in order to provide domestic market security for producers operating close to the margins of international competitiveness rather than to prop up the inefficient. In many respects the policies pursued through to the mid-1970s were in accordance with the government's broad development strategy outlined above. The trade regime was determined by the overriding aim of stimulating agricultural exports and emphasis was placed on maintaining exchange rate competitiveness. Table 4.2 provides some of key indicators of the Malawi economy at the post-independence period before the SAPs.

Malawi had a GDP growth record since the mid-1960s, closely related to growth of agricultural sector. Over 1967-73 period GDP at factor cost grew at 4.6% with agriculture growing at 2.8% during that same period. The GDP accelerated to 6.4% in 1974-78 due to policy of estate expansion and agricultural GDP was also much higher at 5.8% (Table 4.2). After the oil shock of 1979 and the severe drought of 1979/80 crop growing period of Malawi, the GDP growth rate declined to - 0.8% and agricultural growth mirrored the overall growth performance, to a sharp drop of -3.9%. In 1967-73, agriculture contributed 44.4% to Malawi's GDP, falling to 38% by the 1979-81



periods. Meanwhile industry's share remained fairly steady at around 11%. The domestic savings rate was 8.2% between 1967 and 1973 and rose to 18.3 between 1974 and 1978 but declined to 13.2% between 1979 and 1981. Malawi's investment and savings behaviour was closely associated with the growth of estates and other investment financed by implicitly taxing the smallholder sector through a producer price policy.

<b>Table 4.2 Malawi: Economic structure and performance from around Independence</b>			
	<b>1967-73</b>	<b>1974-78</b>	<b>1979-81</b>
Real GDP growth rates (%)	4.6	6.4	-0.8
Per capita GDP growth (%)	2.7	3.2	-0.6
Investment to GDP ratio (%)	20.0	29.6	27.0
Current account deficit to GDP ratio (%)	-11.7	-8.9	-12.7
GDP decomposition by sector (% of GDP):			
Agriculture	44.4	40.8	38.0
Industry <sup>a</sup>	11.0	11.4	11.8
(Manufacturing and Mining)	11.4	11.4	11.8
Infrastructure <sup>b</sup>	11.6	12.6	13.4
Public administration and defence	11.7	8.7	9.8
Others <sup>c</sup>	21.3	26.5	27.0
Average real growth rates (%):			
Agriculture	2.8	5.8	-3.9
Industry	5.3	6.7	2.8
(Manufacturing and Mining)	5.5	6.7	2.8
Infrastructure	8.2	2.6	-2.2
Public administration and defence	0.1	5.7	8.2
Others	5.0	7.6	-2.6
Total savings ratio (%)	8.2	18.3	13.2
Price inflation rate (%)	12.5	8.5	4.0
Real growth rate of imports (%)	8.7	6.1	-4.6
Real growth rate of exports (%)	5.9	-0.7	11.9
<sup>a</sup> Industry includes manufacturing, mining & quarrying and public utilities (electricity, water, sanitary services, etc) <sup>b</sup> Infrastructure includes construction, transport and communication <sup>c</sup> Others include trade, bank/insurance/real estate services and unspecified Source: World Bank - Malawi Country Assessment Evaluation reports, various years			

#### 4.3.1.1 Prices

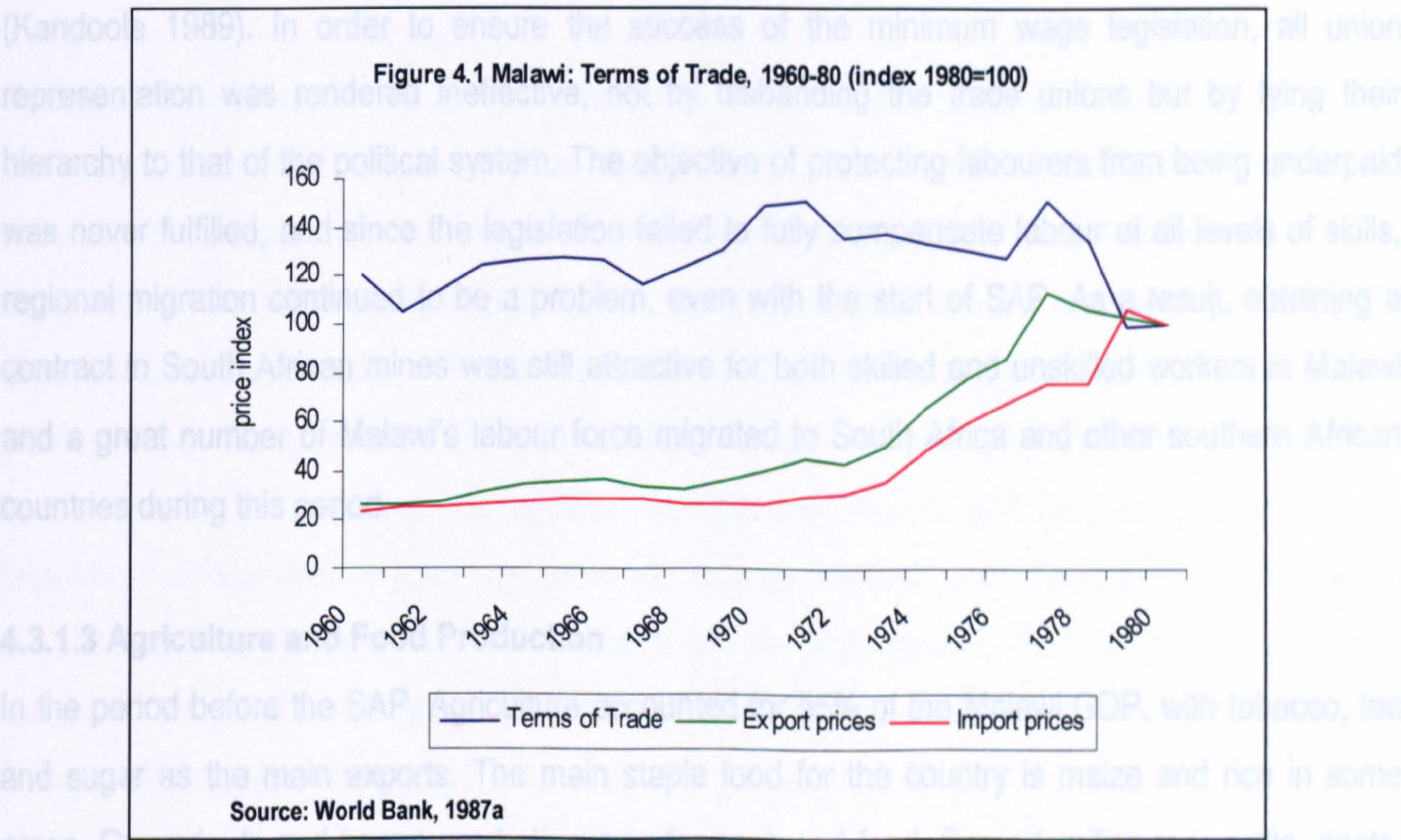
During the high growth period of the 1970s, the average annual inflation rate was about 9%, and this began to change drastically with the intensification of the war in Mozambique. It is not clear what level the rate of inflation was achieved, but it has been officially estimated to be as high as 33% by the beginning of 1989 (World Bank 1990a). While consumer prices were freer, owing to the



strong business lobby behind them, producer prices, particularly for smallholders, were suffering the same downward trends as did real wages in the 1970s. The period between 1977 and 1979 saw the worst downswing as Malawi's terms of trade fell by nearly 35%, as the civil war in Mozambique forced Malawi to use alternative, more costly routes and ports for her exports (Figure 4.1).

#### 4.3.1.2 Incomes, Wages and Employment

Internally, the nature of the growth in agriculture was not analysed, particularly in terms of which sub-sector was stagnating, but much of the decline was due to a drop in tobacco and tea prices, in particular a 36% fall in the 1979-80 auction price of fuel-cured tobacco (Gulhati 1989). Other elements of the decline included a rapid rise in the import prices of capital and intermediate goods and inflation in the countries that were Malawi's trading partners.



It should be noted that ADMARC played a critical role in the pricing of agricultural products in Malawi. ADMARC's mandate was to provide a market for all the crops grown by smallholder farmers by buying at government-approved prices, and was also entrusted with distributing credit to those farmers. However, ADMARC depressed producer prices and transferred the surplus into estate development. Studies commissioned in the early 1980s revealed that part of the stagnation in smallholder output could be explained by the depressed prices at which ADMARC was purchasing that output (Kydd and Christiansen 1982). Since the smallholders had no formal economy suffered major setbacks and this affected the agricultural sector.



channel for lobbying for higher prices, their response was to move out of this unproductive activity and some of them had to lease their land, particularly in the 1980s, and seek paid employment from estate farms. Others avoided having to deal with ADMARC by acquiring the status of an estate, which allowed them to grow burley tobacco and sell it directly on the auction floors.

#### **4.3.1.2 Incomes, Wages and Employment**

Most income in Malawi is generated from the sale of agricultural produce, and the growth of incomes had been restrained by the wage incomes and salaries policy pursued since independence (Ngalande-Banda 1989). The wage incomes and salaries policy had required that all incomes be made uniform, in order to discourage rapid manpower turnover. The effect of this policy has been less than satisfactory in safeguarding against manpower losses to other economies in the region and in ensuring economic stability. The wage restraint policy was intended to stabilise production costs, sustain international competitiveness and generate adequate employment (Kandoole 1989). In order to ensure the success of the minimum wage legislation, all union representation was rendered ineffective, not by disbanding the trade unions but by tying their hierarchy to that of the political system. The objective of protecting labourers from being underpaid was never fulfilled, and since the legislation failed to fully compensate labour at all levels of skills, regional migration continued to be a problem, even with the start of SAP. As a result, obtaining a contract in South African mines was still attractive for both skilled and unskilled workers in Malawi and a great number of Malawi's labour force migrated to South Africa and other southern African countries during this period.

#### **4.3.1.3 Agriculture and Food Production**

In the period before the SAP, Agriculture accounted for 55% of the Malawi GDP, with tobacco, tea and sugar as the main exports. The main staple food for the country is maize and rice in some areas. Groundnuts and beans are both grown for cash and food. Some families rear cattle, goats, pigs, sheep and chicken for food and sale. During the period before economic reversals, maize production was growing at an average rate of 3.2% per annum. The success of agriculture was reflected in other sectors, such as manufacturing, which grew at around 5.5% between 1967 and 1973 rising to 6.7% in the period between 1974 and 1978 (World Bank 1982). The increase in industrial output was due to the introduction of import substitution industries, expansion of domestic demand and export oriented light industries. The results of the agricultural policy during the years following independence were very encouraging up until 1981 when Malawi experienced negative GDP growth rates between 1979 and 1981. With the rise of oil prices in the 1970s Malawi's economy suffered major setbacks and this affected the agricultural sector.



#### **4.3.1.4 The Industrial Sector**

In the thirty years following independence, the Malawi authorities chose a centralised economic approach emphasising state intervention in all sectors of the economy. This interventionist policy of the Malawi government resulted in the nationalisation of most private enterprises and the development of a large number of industrial units under public control, and this period saw the creation of several state monopolies. Thus, the industrial sector was dominated by parastatal monopolies such as the ADMARC, involved in agro-processing industries, the Malawi Development Corporation (MDC) and the Press Corporation Limited (PCL) which was 90% owned by President Kamuzu Banda (Burdette 1990). This highly centralised ownership of the major industries created a situation of state capitalism resulting in a geographical concentration of most establishments located in a few urban centres, and also combined with power and decision-making, wages could be kept low.

Malawi's industrial sector has always consisted of two sub-sectors: agro-processing industries with an export component of tobacco, tea, sugar and cotton-processing industries; and import-substituting producers of intermediate materials and final goods for the domestic market. As in many African countries south of the Sahara, the sector comprises the modern industrial sector recognised by the state and an informal sector operating on the margins of legality. Malawi is not a country with a strong industrial vocation and its comparative advantages are limited and subject to the uncertainty of the climate. In addition, the domestic market and purchasing power of the population are too weak to justify the presence of large industrial units. Another important issue is the nature of linkages between the SME sector and the large-scale formal manufacturing sector. It was found that most SMEs tend to use inputs generated by nature and hence have weak backward linkages with the later (Helmsing 1986).

It can be said that prior to political changes of 1994 the manufacturing and industrial sector of Malawi was divided into two segments. On the one hand, there was a large enterprise group composed of giant multinationals, state enterprises, and heavily protected and subsidised private industries while on the other hand, there was a mass of rural small-scale enterprises, often family run, involved in handicrafts and simple manufacturing. It is these small enterprises who mainly supply rural consumers with simple, inexpensive products made out of local resources.



#### 4.3.1.5 External Debt, Exchange Rate and Balance of Payments

Malawi, like other SSA countries, required extensive resources for infrastructural and other capital projects after gaining independence. Much of the capital was raised by borrowing, which, in the 1960s and 1970s, was mostly concessional. With the onset of the problems of the 1980s, Malawi has had to rely even more heavily on borrowing, this time increasingly on commercial terms. Therefore the sharp rise in international interest rates in the late 1970s and early 1980s represented a severe exogenous shock to the Malawian economy. Malawi's debt service ratio stood at 20.3% over 1978-80 compared to 8% over 1972-74 (Gulhati 1989). However, throughout the 1970s, when the real growth of the economy was significant, Malawi's debt remained small compared to the 1980s and 1990s.

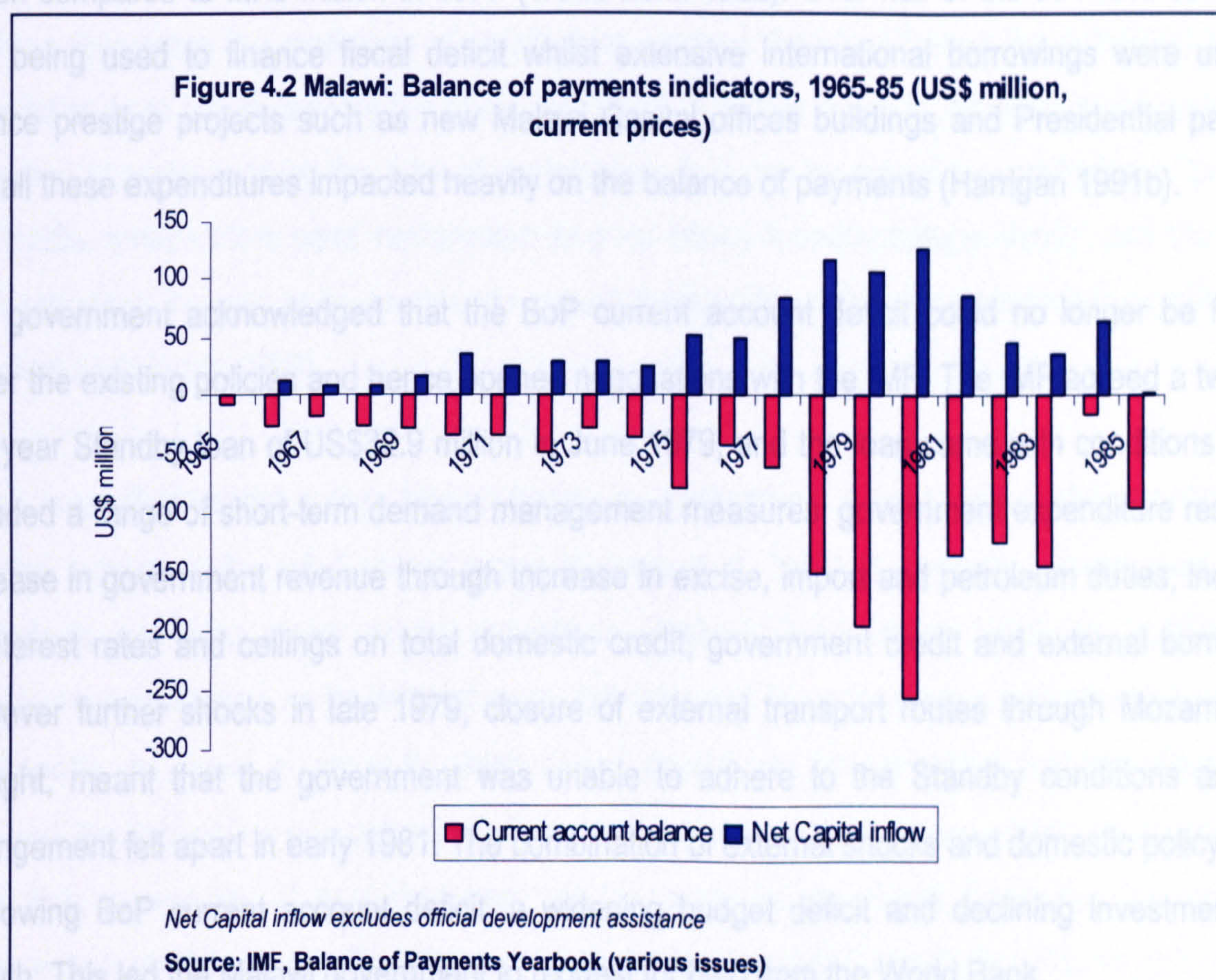
Immediately after its independence from Britain, Malawi adopted its own currency, the Malawi *pound* which was pegged to the British pound sterling. In 1971, a new, decimalised currency known as the *kwacha* was introduced, which was initially pegged at 2 *kwacha* to the pound sterling. In 1973, following the floating of the pound sterling, Malawi switched to a basket pegging regime (Harvey 1983). The purpose of pegging was to avoid wide fluctuations of the *kwacha* exchange rate. The Malawi *kwacha* (MK) was de-linked from the *pound sterling* and initially pegged to a trade-weighted basket of the British pound and US\$ up until 1975 when it was pegged to IMF's Special Drawing Rights. From 1984 to 1994 the MK was tied to a weighted basket of currencies of Malawi's then seven major trading partners: US dollar, British pound sterling, German mark, South African rand, French franc, Japanese yen, and the Dutch guilder (before the introduction of the Euro currency). After 1994 the foreign exchange market was completely liberalised and the MK was allowed to float freely according to forces of demand and supply (RBM 2000).

With regards to balance of payments indicators, like many other developing countries, Malawi registered deficits in its BoP in the current account throughout the post-independence period. Up to the middle of the 1970s, these negative balances were usually adequately offset by long-term capital inflows (Kydd and Hewitt 1986a, b), but the deficits had been growing over the years. The first sign of a weakening in the external sector came at the outset of the 1978-81 crisis, when the BoP current account deficit exploded from US\$61.7 mill in 1977 to US\$150.1 million in 1979 and to US\$257 million in 1981 (Figure 4.2).

Overall, it can be said that the Malawi economy was relatively healthy up until the late 1970s. It can be said that it was during the period between 1964 and 1978 that Malawi experienced some



economic success (Acharya 1981). The strong economic performance was attributed to a successful pursuit of an export-oriented, agro-based, labour-intensive development strategy under which import-substituting industrialisation played a secondary role. Policies implemented in pursuit of this strategy included: public sector investment in physical infrastructure, maintenance of a competitive exchange rate, low tariff levels, restraint of wages and income increases with a lead coming from the public sector, encouragement of foreign capital and restrained fiscal and monetary policies in order to contain inflation and preserve international competitiveness.



#### 4.4 The Economic and Political Reforms (1981 onwards)

##### 4.3.2 The period of economic crisis, 1979-81

The positive assessment of the Malawi economy was short-lived, owing to external events that began in 1979. Increases in world oil prices and war in Mozambique destabilised the economy. At the same time failure to reverse stagnation in the smallholder sub-sector of agriculture made the economy vulnerable to external shocks, as it could no longer fall back on this sub-sector (Kydd and Christiansen 1982). Consequently, output plunged, and for the first time since independence GDP registered negative growth rates from the mid-1980s. It is evident that 1979 marked the end of a period of strong economic growth and the beginning of a period of economic difficulties.



A fall in the price of tobacco, Malawi's major export product (Pryor and Chipeta 1990), on the world market coincided with an intensification of the war in neighbouring Mozambique, cutting Malawi off from its access to the sea and increasing transport costs. Furthermore, interest rates on foreign commercial loans increased substantially and a partial drought in the southern part of the country caused a decline in earnings from food exports and forced the Malawi government to spend scarce foreign exchange on food imports. However, government revenue failed to keep pace with the growth of expenditure and resorted to domestic borrowing, which by 1980 amounted to MK62 million compared to MK9 million in 1977 (World Bank 1982). Over half of the domestic borrowing was being used to finance fiscal deficit whilst extensive international borrowings were used to finance prestige projects such as new Malawi Capital offices buildings and Presidential palaces, and all these expenditures impacted heavily on the balance of payments (Harrigan 1991b).

The government acknowledged that the BoP current account deficit could no longer be funded under the existing policies and hence opened negotiations with the IMF. The IMF agreed a two and half year Standby loan of US\$32.9 million in June 1979, and the loan came with conditions which included a range of short-term demand management measures: government expenditure restraint; increase in government revenue through increase in excise, import and petroleum duties; increase in interest rates and ceilings on total domestic credit, government credit and external borrowing. However further shocks in late 1979, closure of external transport routes through Mozambique, drought, meant that the government was unable to adhere to the Standby conditions and the arrangement fell apart in early 1981. The combination of external shocks and domestic policy led to a growing BoP current account deficit, a widening budget deficit and declining investment and growth. This led the Malawi government to request for help from the World Bank.

#### **4.4 The Economic and Political Reforms (1981 onwards)**

The World Bank, through its diagnostic work on the macroeconomic disequilibria and structural problems of Malawi, identified six structural weaknesses in the economy: the slow growth of smallholder exports; the narrowness of the export base, in particular the increased reliance on tobacco; dependence on imported fuel and on a declining stock of domestic fuel wood; the rapid deterioration in parastatal finances; the increasing budget deficits of the late 1970s; and the inflexible system on government administered prices and wages (World Bank 1981b). The Malawi government's strategy for tackling the crisis that emerged in 1979 proved inadequate as it failed to bring about the necessary reforms in areas such as the marketing of agricultural produce and the investment strategies of some industries. And it was with this backdrop that Malawi was prescribed



the economic policy reforms by the World Bank and IMF, under the banner of Structural Adjustment Programme.

The major thrust of the macroeconomic policies since the 1980s has been directed at restructuring the economy. The policies that are now in place can best be characterised as driven by the SAP. They cover three broad areas: agriculture, industry and the external sector. Policy changes in agriculture began in 1982, when the handling of produce by the ADMARC came under reform. The new policies, which were intended to make the smallholder sub-sector a more vibrant economy, involved liberalising the marketing of smallholder produce thereby allowing the ADMARC to face competition from private traders (Scarborough 1990). A further move in the agricultural sector was relaxation of restrictions on the type of export crops that can be grown by smallholders. Until the mid-1980s, smallholders were not allowed to grow burley tobacco independently, and the World Bank proposed the new policy in order to spread the benefits of this lucrative crop to smallholders (Patchett and Harnet 1990).

In the area of industrial policy, Malawi began to aggressively pursue one of the most market-oriented regimes in the sub-Saharan region (Kaluwa et al. 1991). It gradually relaxed most import restrictions and also some export restrictions (Malawi Government 1998). In addition, the Government developed an investment code that intended to encourage entrepreneurs who have the capacity to invest in areas in which export goods can be generated and incentives were provided for indigenous entrepreneurs. Since the major constraint facing small entrepreneurs is cash flow, a number of agencies were set up, such as the Small Enterprise Development Organisation of Malawi, the Development of Malawian Traders Trust (DEMATT) and the Malawi Union of Savings and Cooperatives, all aimed at assisting indigenous entrepreneurs to break into various types of industries (Scarborough 1990).

In the external sector, foreign exchange was liberalised. Firms no longer had to apply for foreign exchange through the Reserve Bank of Malawi (Malawi Government 1998), and this role was passed on to the Commercial Bank. The growing and manufacturing of export commodities were encouraged, and the exchange rate was being managed in such a way as to maintain stability and retain Malawi's competitiveness (Malawi Government 1998). Macroeconomic policies were thus geared to making Malawi more market oriented and competitive, both internally and externally. These policies are extensions of the market-oriented policies of the IMF and the World Bank, implemented by means of the loans that the country received.



The reform efforts were supported by World Bank lending from 1981 to 1990 through three Structural Adjustment Loans (SALs) and two Sectoral Adjustment Loans (SECALs) for Industry and Trade Policy (1988) and Agriculture (1990), and by four IMF Stand-by or Extended Fund Facility and Enhanced Structural Adjustment Facility (ESAF) arrangements from 1979 to 1995. In 1996 another form of SAP, supported by the World Bank, the Fiscal Restructuring and Deregulation Programme (FRDP) was approved for Malawi. All these reform measures are further discussed in turn in the following sub-sections.

#### **4.4.1 Structural Adjustment Loans**

The World Bank supported the SAP through provision of three consecutive Structural Adjustment Loans between 1981 and 1987, which carried economy-wide reform conditions (Cromwell 1992). The reform conditions were to target five general objectives: improvement of the BoP position; adjustment of price incentives and income policy; strengthening resource management; rationalising the government investment programme; and institutional improvements (World Bank 1981b). A more detailed presentation of the SAL programme in Malawi is given in the Appendix 1.

Malawi's first SAL was approved in June 1981 and provided US\$45 million for the period 1981-84. This loan was intended to solve problems related to agriculture, BoP and resource management and also to improve the management and financial practices of key institutions in the public and private sectors. For BoP position, SAL I emphasis was placed on increasing smallholder export crop production which was to be achieved through annual reviews of smallholder producer prices in order to increase prices towards export parity levels. The contribution of agro-industry to BoP was to be achieved through reforms of the MDC and Press Holdings, to enable them to undertake new investments. Studies were also commissioned on efficiency of ADMARC marketing and storage operations. In terms of price incentives and income policies, the Malawi government was required to carry out a review of the price control system to improve its flexibility and carry out more frequent parastatal tariff increases in line with cost increases. With regards to resource management reform, the government was to look at its budget and see if it could increase its revenues including a 15% increase in all specific excise and import duties (World Bank 1981b). For SAL I, a large number of conditions related to the conducting of studies, reviews and plans which were to provide inputs to subsequent SAL operations.



SAL II was approved in December 1982 for US\$55 million for the period 1984-86. The second SAL incorporated findings of some studies conducted under SAL I. The government was asked to revise the estate extension and management training programme under SAL I. Specific conditions on consumer price de-control were defined, placing emphasis on measures to increase government revenues. Under SAL II, price de-control was carried out on a substantial number of items. In addition, the Department of Statutory Bodies was required to carry out an annual review of parastatal finances and implement tariff increases where necessary. A new condition added under SAL II was the removal of government subsidy on smallholder fertilisers. There was to be a 60% reduction in fertiliser subsidy supplied by ADMARC to smallholders in 1984-85 and subsidy elimination by 1985-86. Under Extended Fund Facility programme with IMF, the government was asked to devise specific measures to improve buoyancy of the tax system and government revenue to remain at the current ratio with respect to GDP. In order to assist with public sector resource management, a review of the annual Public Sector Investment Programme (PSIP) with the Bank staff was to be carried out. The government's system for external debt monitoring was required to be operational and a borrowing strategy developed in order to achieve a 20% debt service ratio (World Bank 1981b).

SAL III was approved in December 1985 for US\$70 million for the period 1986-87. In many cases the third SAL represented a continuation of the policies initiated under previous two adjustment loans. The government was to continue reviewing crop and input prices, and fertiliser subsidies were to be phased out. The programme of consumer price de-control was to be completed by the end of 1985. A three-year PSIP, revenue and expenditure projections, and external borrowing plan were to be reviewed by the Bank, and also active exchange rate management was to be maintained. In addition to continuation of previous measures, a restructuring of the tax system, with initial changes to be implemented in the 1986-87 budget, was to be carried out; measures to stimulate competition and exports within the industrial sector were to be put in place; ADMARC's role was to be redefined along with attempts to stimulate private trading in smallholder agricultural markets; and government budget required to be given a 'programmatic content', emphasising performance and output (World Bank 1981b).

#### **4.4.2 Sectoral Adjustment Loans**

In 1987 a proposed fourth SAL idea was abandoned due to the failure of SALs I - III to generate sustainable growth, and a new approach to adjustment lending, the Sectoral Adjustment Loans (SECAL) to be signed off by 1990, was proposed. This was to address some of the country's more



deeply rooted structural problems and was thought to be a much more integrated approach to policies than the SALs (Mosley et al. 1991). The adjustment initiatives were to come from the Malawi government itself, supported by, rather than imposed, by the World Bank. The government realised that the estate-led export expansion and import-substitution policies no longer offered a viable development strategy. SECAL commenced in 1988 and to begin with was granted to the Trade and Industry sector under the Industrial and Trade Policy Adjustment Credit (ITPAC). It was acknowledged that price liberalisation needed to be closely sequenced with trade liberalisation in order to stimulate competition and to increase the private manufacturing sector's contribution to export revenues (World Bank 1989e).

Policy measures were aimed to put exporters in a free-trade position to reduce the general tariff level, and also a comprehensive tax reform structure was undertaken to facilitate the export drive. There was no official programme for Malawi to follow although the government was expected to reduce the fiscal deficit through increased taxes and tariffs; limit civil service wage bill; reduce capital expenditures; and improve budgetary monitoring under the IMF shadow programme. This programme included a 20% devaluation of the *Kwacha* in February 1987 and a further 15% in January 1988. When the ITPAC commenced, it included the initiation of an import liberalisation programme; elimination of import and export licences on various goods; removal of exclusive protection clauses in the Industrial Development Act; and implementation of the first phase of a tax reform programme.

The principal aim of ITPAC was to change the market structure of the industrial sector by increasing competition. This reflected the Bank's acknowledgement that previous SAL reforms, in particular the strengthening of companies such as Press and MDC, had intensified the sector's import-intensive oligopolistic structure (World Bank 1987c). SALs, with their emphasis on agricultural export-led growth, had generally ignored the potential to forge internal market linkages using the industrial sector. The central component of ITPAC was trade liberalisation, complemented by: flexible exchange rate management and reform of foreign exchange allocation; gradual fiscal deficit reduction and tax reform; further price control; export and small-scale enterprise promotion and increased efficiency in the financial sector.

Major liberalisation of the trade regime under ITPAC took place via a phased three-year liberalisation of the foreign exchange allocation system, which removed the need for prior foreign exchange approval for a wide range of imports. The liberalisation covered most raw materials,



spare parts, intermediate and capital goods, and a limited range of consumption goods. To support the trade liberalisation, the government also agreed to expand the Open General License system beyond a list of 85 imports covered in mid-1988. Hence, certain categories of goods and goods from certain countries would no longer require import licenses from the Ministry of Trade, Industry and Tourism. Both the Bank and Fund accepted that the three year import liberalisation programme would place pressure on the BoP Current Account and regarded the ITPAC credit, its co-financing which amounted to US\$170 million, as key resources to help bridge the associated finance gap (World Bank 1988d).

A comprehensive tax reform programme was also undertaken which involved rationalising trade taxes so as to reduce domestic protection and encourage efficient production. The broader aim of the reform programme was to shift the burden of taxation from international trade and production to domestic trade and consumption. Some analysts believe that, by 1990 this tax reform programme had successfully lowered tax rates and raised tax revenue as a percentage of GDP (Shalizi and Thirsk 1990).

Other ITPAC measures designed to increase domestic market competition included: revision of the government's Industrial Development Act to eliminate clauses which guaranteed exclusive monopoly rights in certain production activities; decontrol of prices on low grade meat and petroleum; and a commitment to strengthen the resource base and institutional support for small-scale off-farm industries. The final element of ITPAC concerned financial sector policies. Monetary and credit policies were to be monitored by the IMF whilst government agreed, under ITPAC, to undertake reforms to strengthen the financial sector. These included: updating and strengthening the financial system's legal framework; improving mobilisation of domestic long-term funds; and making credit more accessible to small-scale industry. Trade liberalisation aimed to ensure a competitive manufacturing base which would make use of Malawi's relative labour abundance, particularly through the promotion of small and micro scale industries.

In 1990 ITPAC was followed by a second SECAL, the Agricultural Sector Adjustment Programme (1990-92 period). The Agricultural Sector Adjustment Credit (ASAC) provided a total of US\$170 million conditional loan and acknowledged that previous adjustment efforts had failed to address the policy bias within the agricultural sector against smallholders. Much of the bias had intensified during the earlier adjustment period as reflected in land reallocation and cropping restrictions and in relative price, tax and investment trends (World Bank 1990c). ASAC proposed the increase in land



rents in the estate sector and removal of the legal restrictions against smallholder production of burley tobacco, an export crop previously reserved for estate production.

#### **4.4.3 Extended Fund Facility and Enhanced Structural Adjustment Facility**

When the World Bank's SALs and SECALs were being proposed and implemented, other measures such as the Extended Fund Facility under the IMF Stand-by programme were already running in the country. The main objectives of these facilities were to restore a macroeconomic balance and to improve economic growth and efficiency (Sijm 1990). The IMF-supported stabilisation measures in the early stages were aimed at reducing the budget deficit from 9.6% of GDP in 1979 to 6.8% in 1981 and cutting back volume of imports by 14%. In 1982, the IMF-supported programme attempted to further reduction of the persistent financial imbalances through revenue enhancement, partial freezing of public sector employment, and phasing out fertiliser subsidies. In addition the government agreed to further devalue the *Kwacha* and seek rescheduling of its public and private debt. With the help of a three-year IMF extended facility in 1983, emphasis shifted from stabilisation to a more balanced mix of demand restraint and supply-side measures. These included: government expenditure declines; wage freeze; elimination of fertiliser subsidies; slight increases in revenue/GDP ratio and import volume. Public finance was to be restructured through improved budgeting planning, improved profitability and efficiency of parastatals, increased revenue from taxes, utility rates and fees for public services.

In 1986, the IMF introduced a Structural Adjustment Facility and subsequently the Enhanced Structural Adjustment Facility, both offering highly concessional disbursement over a three to four-year period to low-income less developed countries. Malawi received its first ESAF in 1988 for the period 1988-94. The focus of the programme was partly fiscal and partly structural, and the fiscal objective was to reduce government expenditure. Structural objectives included liberalisation of foreign exchange; productivity gains in smallholder agriculture; reform of agricultural marketing; and financial liberalisation. For the smallholder sector, the intention was to raise producer prices, increase fertiliser use and lift restrictions on entry into cash crops.

Another credit facility implemented was the Entrepreneurship Development and Drought Recovery Programme (EDDRP) in the period 1992-95. This aimed to create a favourable environment for enterprise development and focused on tax incentives and measures to enable the country to cope with problems of drought. It was initiated mainly to mitigate drought effects of 1992 through a supplementary provision. The Industrial Development Act was repealed and replaced with the



Industrial Licensing Act of 1992. Investors and entry onto the manufacturing sector no longer required manufacturing license except for a few chemical products. Credit allocation was abolished, interest rates were liberalised, tariffs were reduced and rates consolidated. This opened up the economy and increased the degree of import competition from manufactured products.

In 1995 the Malawi government adopted a second ESAF programme which envisaged rapid fiscal adjustment and government expenditure. Structural reforms for this programme included privatisation of public enterprises, civil service reforms, elimination of restrictions on smallholder access to land and cash crops and liberalisation of agricultural marketing.

#### **4.4.4 Fiscal Restructuring and Deregulation Programme**

The first FRDP for Malawi was approved in 1996 and its main objective was to support adjustments in public sector and social sectors particularly on improving the efficiency of the civil service, improving public expenditure control and rationalisation of tariff and surtax administration. The programme also involved an enactment of the Export Processing Zones Act in 1995 as an institutional framework for the promotion of both domestic and foreign investment. The programme was also to focus on removal of remaining pricing and marketing constraints on smallholder agriculture as well as constraints on private sector development. Improved access to cash crops and alternative markets was expected to increase smallholder household incomes, and exporters were expected to gain from increased incentives for agricultural diversification, helping the economy reduce its dependence on tobacco from 66% to 50% by 2005 (World Bank 1996a). There were three FRDPs, implemented in Malawi, between 1996 and 2000.

It should be noted that some programme activities between the WB and IMF were overlapping. Traditionally, IMF concentrated on short-term demand management to stabilise the economy using policy instruments such as the real exchange rate, credit ceilings and interest rates, whilst the Bank concentrated on medium-term supplied-side policies to change the structure of the economy so as to generate sustainable growth using policies such as price, market and trade liberalisation. This became more blurred during the 1980s, as the Fund increasingly used its extended facility which allows for disbursement of loans over three years and repayment periods of up to ten years, in contrast to normal Stand-by loans disbursed over a year (Bird 1995). And can be seen from the discussions above, the IMF also had measures which were touching on some issues relating to smallholder sector, fertiliser subsidies, civil service reforms, which one would presume that they were tackled under the Bank's SALs or SECALs. It has been pointed out that this overlap in



measures may have caused problems in terms of time horizons and objectives (Morsley et al 1991).

#### **4.4.5 Political transition and economic liberalisation**

Malawi, like many other SSA countries, was caught in a worldwide "new wave" of political liberalisation of the early 1990s, following the collapse of communism in 1989. The great dependence of Malawi on external Aid meant that it had to pay attention to demands from major donors, notably USA and Europe (linking 'aid' to 'good governance'). Donors were deeply concerned with lack of progress in the area of basic freedom and human rights in Malawi, and accordingly stressed the need for early implementation of appropriate reforms. Henceforth, Malawi had to pursue political and economic liberalisation simultaneously.

Political transition evolved rapidly and a new democratically elected government, led by the UDF came into power in 1994. However, while the new government largely respected the rule of law and the fundamental freedoms of expression and association, its political management was thought to be weak and administrative performance was rendered poor by the WB (World Bank 1997b). In addition, the agricultural credit system had collapsed, maize production profitability was in decline, the estate agricultural sector was in disarray, industry faced intense competitive pressure from imports, and infrastructure was dilapidated. However, peace in Mozambique, democratic transition in South Africa and in Malawi itself and the chance for a new government to take stock of the past reform process and in the light of lessons learnt devise a new strategy placed the country on the cusp of change and offered new opportunities (World Bank 1997a).

With regard to economic liberalisation, the economy had several features that needed to be liberalised. For example, the previous head of government still personally owned Press Corporation Company that controlled about 30% of the national economy. There was also the case of numerous state enterprises that were subsidised, in varying degrees, by the state budget. Although the previous government showed willingness to move ahead with economic liberalisation, paying due attention to the importance of macroeconomic stability, the macroeconomic fundamentals were not fully in place. Fiscal reform was inadequate, trade reform was not comprehensive, restructuring of parastatals was initiated but privatisation was ad hoc, and ownership was still distorted. Given that the country depends on international institutions and other donors for BoP support, the new government had little choice but to continue with the liberalisation and privatisation drive. However,



it clearly distinguished itself from the previous regime by placing poverty alleviation at the centre of its economic and social agenda (Government of Malawi 1998).

In the early years of the new regime both the government and the World Bank were able to take stock of the past adjustment effort and derive important lessons. Both clearly judged past efforts to have failed, since the adjustment had failed to change the structure of production and exports. The Bank judged disappointing performance to have resulted from a combination of policy failure and exogenous shocks (World Bank 1997a). One of the key lessons highlighted by the Bank was that the old regime had failed to adequately remove pervasive barriers to entry in markets thereby discouraging private sector investment and growth. In response the UDF promised to deepen and accelerate the liberalisation and privatisation effort. The aim was to improve efficiency, redistribute wealth, create employment, increase investment and technical change and improve competition and micro and small enterprise policy (Government of Malawi 1998).

Although agriculture, especially the smallholder sector, was still regarded as important it was acknowledged that in view of population pressure on land, structural transformation was essential. Exclusive reliance could not be placed on agriculture to reduce poverty. Instead, off-farm incomes would be crucial. The new government placed particular emphasis on the development of manufacturing, tourism and mining to bring about the much-needed diversification. At the same time the interdependence of farm and off-farm activities was acknowledged. The strategy had broad-based poverty reducing growth as its principal aim, to be achieved via smallholder development and diversification, particularly off-farm activities. The private sector and competitive markets were to provide the engine of growth with a reduced role of parastals and state-sponsored private oligopolies (World Bank 1996b). Instead, the role of the state was to promote the private sector whilst supporting social development. The later was to be achieved by a re-orientation of public expenditure and the introduction of more safety net programmes. To provide a framework for the above the government promised to follow sound macroeconomic policies, in particular, control of the fiscal deficit and a competitive exchange rate policy (Government of Malawi 1999c).

Tariffs were reduced further, and in terms of exchange rate policy the key aim was to restore international competitiveness to boost exports and encourage diversification. This was assisted by the removal of the export licensing system. Attempts to reduce inflation were also central to the external competitiveness policy, and the government introduced fundamental reform in exchange rate policy. The *kwacha* was floated with the old currency pegging replaced by market-determined



auction rate. At the same time all restrictions on external current account transactions were removed and restrictions on capital movements by non-residents liberalised.

#### **4.5 Impact of the reform measures**

The following sections discuss the macroeconomic impact of the SAP and economic reforms on the Malawi economy as a whole, and then briefly discussing the impact on the smallholder, estate, external, industrial and SME sectors of the economy in turn. The impact is discussed within the context of the measures themselves, rather than separating out impact of World Bank's and IMF's measures, as it is too complex to separate them out. Although the SAP for Malawi was first approved in June 1981 by the WB, implementation was not in place until 1982. It should be noted that in this study the period before 1981 is taken to be the pre-adjustment period but the discussion of the adjustment impact covers the period from 1982 as that was the year when the first SAL was actually implemented in the country.

##### **4.5.1 Impact on the Malawi economy as a whole**

During the period 1982 to 1987, when the SAP was in place, the Malawi economy showed some signs of improvement as a result of higher export prices for tobacco. However, because of bad weather conditions in 1987 and influx of Mozambique refugees, crop production was disrupted and this led to food shortages in some parts of the country such that food had to be imported from other countries. Although food production was high in the 1970s and 1980s, some studies have shown that there have been chronic food shortages at household level even in years of good harvest (Malawi NSO 1992).

Intensified land cultivation has led to deteriorating of soil fertility such that fertilizers have to be used to increase production. In Malawi, fertilizer is imported and farmers have to either buy it or get it on loan from the government, and it is difficult for most smallholder farmers to obtain fertilizer and hybrid seeds on credit with the end of fertiliser subsidy policy. The 1991 National Sample Survey of Agriculture (NSSA) showed that only 19% of households with less than 0.7 hectare of land were using fertilizer while those with holdings between 0.7 and 1.49 hectare, only 33% used fertilizer (Malawi NSO 1992). These other factors affected the agricultural output growth, despite the SAP.

Although the agricultural sector growth rate was negative (-3.9%) during 1979 to 1981 period (Table 4.2), it was restored to 6.3% in 1984, contributing to the real GDP growth rate of 2.1% during that year. It has been argued elsewhere that much of the GDP growth rate recovery in 1982-84 resulted from domestic policy initiatives which were independent of the SAL programme (Mosley et



al. 1991). For instance 1981-82 saw an upturn of estate performance (a sector which was largely ignored by the SAL policies), resulting from government's own solution to the financial and managerial problems facing a large number of tobacco estates in the late 1970s, which contributed to the favourable GDP growth rate during that period. There was also a sharp increase in maize producer prices by the government, in violation of SAL I condition, which was also a major factor in recovery of the growth rate in the smallholder sector.

Following 1984, the economic recovery stalled as GDP declined to 3.6% in 1985 as the agriculture output growth fell to -9.7% in that same year (Table 4.3). Under SAL II, the government was unable to continue with its own smallholder pricing policies. The SAL policies of suppressing maize producer price and input subsidy (fertiliser) removal, gave rise to a rapid deterioration in smallholder performance, hence the sector's decline to contribute to GDP growth, and in addition there was a need for massive imports of maize.

Table 4.3 Growth rates of GDP and its components, 1982-1986				
	1982-84	1984	1985	1986
Real GDP growth rates (%)	4.6	7.6	3.6	1.06
Average real growth rates (%):				
Agriculture	5.8	6.3	-9.7	0.9
Industry <sup>a</sup>	3.4	3.7	0.5	3.2
(Manufacturing and Mining)	3.4	3.4	0.5	0.9
Infrastructure <sup>b</sup>	0.8	-5.6	18.9	-2.8
Public administration and defence	7.7	2.8	6.1	-0.1
Others <sup>c</sup>	5.1	3.3	2.2	2.5
<sup>a</sup> Industry includes manufacturing, mining & quarrying and public utilities (electricity, water, sanitary services, etc) <sup>b</sup> Infrastructure includes construction, transport and communication <sup>c</sup> Others include trade, bank/insurance/real estate services and unspecified Source: World Bank, Malawi Country Assessment Evaluation reports, various years				

In addition to descriptive policy measures, there were also numerical projections for key macroeconomic variables as expected outcomes of the reform conditions associated with the loans (World Bank 1981b, 1983, 1985). The projections were drawn up by Bank mission staff in collaboration with Malawian Ministry of Finance staff and Malawi Economic Planning Development Division.

Table 4.4 presents the planned outcomes of the adjustment programme compared with the actual outcomes achieved in the period 1982-88. Some of the indicators in Table 4.4 have been presented in Figure 4.3 for illustration purposes and as can be seen, the overall results are not favourable.



Growth rates of GDP, agricultural output and gross investment, all fell short of the planned outcomes and the shortfall was particularly large in the case of GDP growth, which was much less than what the Bank had predicted. Similarly, actual outcomes for the budget deficit and the import and export growth rates fell short of target by significant margins. The actual performance of both merchandise exports and imports also fell short of programme targets over the 1982-88 period. Only in the case of BoP current account deficit and the share of Government development expenditure in GDP, did the actual outcomes of the three SALs achieve the targets set. The GDP reached 7.6% in 1984 matched by increase in export growth from -8.6% in 1982 to 32.5% in 1984, combined with decrease in import growth in 1984, resulting in a reduction in the BoP current account deficit from US\$125 million in 1982 to US\$16.5 million in 1984 (Table 4.4).

**Table 4.4 Comparison of Planned to Actual Outcomes of Malawi's Adjustment Programme, 1982-88**

	Planned Outcomes							
	1982	1983	1984	1985	1986	1987	1988	
GDP growth (%)	14.7	2.6	3.0	3.5	3.4	3.6	3.7	
Agricultural growth (%)	N/A	2.7	3.2	3.6	3.3	3.4	3.5	
Gross investment growth (%)	N/A	20.2	13.7	9.8	3.4	2.8	3.9	
Budget deficit (% of GDP)	N/A	N/A	N/A	N/A	7.5	n/a	n/a	
Development expenditure (% of GDP)	N/A	N/A	N/A	N/A	9.0	n/a	n/a	
Balance of payments current account deficit (current US\$ mill)	254.0	156.6	170.3	180.4	128.9	116.1	107.9	
Merchandise exports growth (%)	15.6	6.4	6.1	4.8	4.5	5.0	5.3	
Merchandise imports growth (%)	12.7	14.2	5.4	4.9	3.0	2.7	3.0	
	Actual Outcomes							Assessment
	1982	1983	1984	1985	1986	1987	1988	
GDP growth (%)	2.5	4.4	7.6	-7.5	7.9	2.5	-2.4	not achieved
Agricultural growth (%)	6.9	4.3	6.3	-9.7	7.8	2.2	-1.7	not achieved
Gross investment growth (%)	24.1	14.7	-28.4	35.3	-37.0	30.1	11.6	not achieved
Budget deficit (% of GDP)	n/a	n/a	n/a	n/a	12.5	n/a	n/a	not achieved
Development expenditure (% of GDP)	n/a	n/a	n/a	n/a	8.7	n/a	n/a	achieved
Balance of payments current account deficit (current US\$ mill)	125.0	144.2	16.5	16.8	75.1	55.0	53.1	achieved
Merchandise exports growth (%)	-8.6	4.3	32.5	19.5	-0.9	12.4	6.6	not achieved
Merchandise imports growth (%)	-18.7	0.1	-12.1	1.4	-13.1	15.5	42.5	not achieved

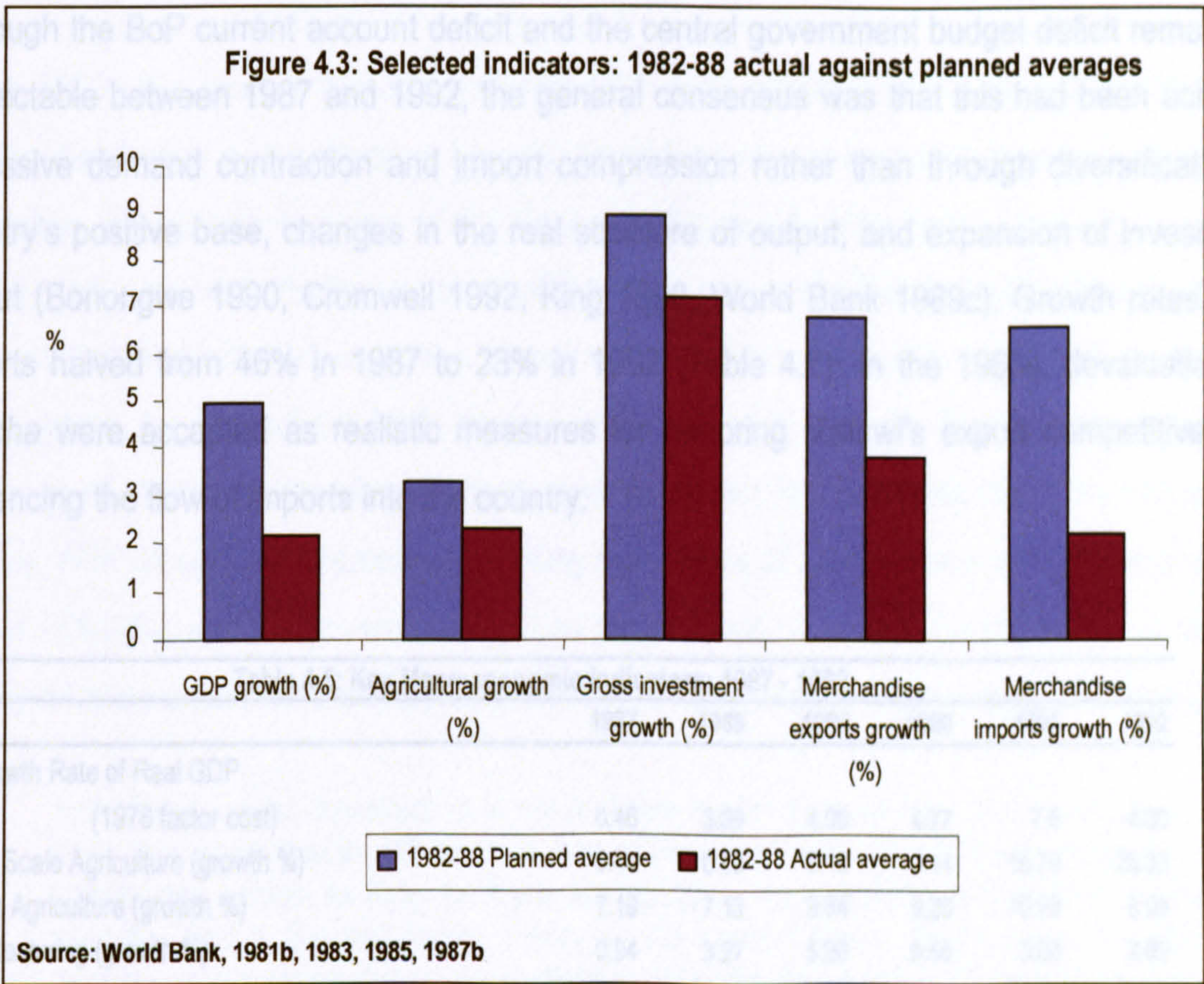
Source: World Bank, 1981b, 1983, 1985, 1987b

N/A = not available; n/a = not applicable

The IMF claimed that the improvement in the deficit was attributable to the 'successful' implementation of the structural adjustment programme and the restriction on imports in the 1980s



(IMF 1998). The latter was implemented by foreign exchange allocation and the requirement that importers deposit 25% of the value of imports with the Reserve Bank at the time they placed their orders. A further factor that contributed to the improvement in the trade balance was the increased merchandise exports, in particular export earnings from tobacco in the 1984 (Patchet and Harnet 1990).



Ad hoc tax increases, combined with parastatal tariff increases, temporarily boosted government revenue and played an important role in the improved fiscal performance whilst the SAL-guided improvement in budget preparation reduced government expenditure, in 1982-88. However, the ad hoc tax increase measures were having disincentive effects in private investment, and the reduction in government expenditure resulted in cut backs in development expenditure, hence there was an overall reduction in investment levels. However, despite underachievement in most targets, the system of budget preparation was greatly improved upon as was government external debt monitoring capacity. The Department of Statutory Bodies was strengthened, enabling the parastatal sector to become increasingly integrated into the central government's financial planning, and MDC and Press were both successfully restructured (Mosley et al 1991).



With regards to debt, it was believed that the acceleration in the accumulated external debt was brought about partly to finance the SAP. Debt service as a percentage of exports was only 8.7% in 1978, but by 1987 it was nearly half of the exports (about 49%) and represented nearly 11% of the GNP (Government of Malawi 1993). By 1987 the total debt stood at US\$1,363 million which is nearly four times what it was in 1978 (Kaluwa et al. 1991).

Although the BoP current account deficit and the central government budget deficit remained fairly respectable between 1987 and 1992, the general consensus was that this had been achieved via excessive demand contraction and import compression rather than through diversification of the country's positive base, changes in the real structure of output, and expansion of investment and output (Bonongwe 1990, Cromwell 1992, King 1990, World Bank 1989c). Growth rates of visible imports halved from 46% in 1987 to 23% in 1992 (Table 4.5). In the 1980s, devaluations of the *kwacha* were accepted as realistic measures for restoring Malawi's export competitiveness and influencing the flow of imports into the country.

Table 4.5: Key Macroeconomic Indicators: 1987 - 1992						
	1987	1988	1989	1990	1991	1992
% Growth Rate of Real GDP						
(1978 factor cost)	0.46	3.29	4.06	4.77	7.8	-4.00
Small Scale Agriculture (growth %)	-0.86	0.50	0.16	-3.44	15.79	-25.33
Estate Agriculture (growth %)	7.19	7.13	9.84	9.20	10.98	8.99
Manufacturing (growth %)	0.94	3.27	5.00	8.50	3.00	2.69
Investment % of GDP	15.40	18.70	20.20	19.10	20.20	19.80
Balance of Payments:						
Current Account Deficit (US\$ billion)*	-0.03	-0.02	-0.14	-0.06	-0.15	-0.23
Growth Rate of Exports (%)	33.13	22.19	3.29	54.48	22.70	2.30
Growth Rate of Imports (%)	45.94	65.22	20.44	22.01	26.90	23.20
Government Deficit as % of GDP	-7.43	-2.07	-2.10	-4.20	-2.30	-3.2
Government Development						
Expenditure as % of GDP	9.24	9.47	6.70	6.10	6.60	6.90
Price infaltion rate %	26.80	31.40	15.70	11.50	11.90	22.70
Source: Malawi Government Economic Report, various years						
*IMF, WEO database, Sept 2006. Different source used as Malawi Government reported the balance in MK						

Another overriding objective of the devaluation was to comply with the requirements of the SAP. It was also thought that devaluations might encourage diversification away from traditional exports towards non-traditional exports. All indications are, however, that such diversification has not occurred and that the country still relies on its three traditional exports (tobacco, tea and sugar) for more than 90% of her export earnings (Malawi Government 2005b). Failure of the SALs objective



of diversifying the predominant agricultural production base was shown by the fact that the share of the three leading exports (tobacco, tea and sugar) in total rose from 77.7% in 1981 to 83.0% in 1988 (Chalira 1993). In addition, the industrial sector remained import intensive (World Bank 1988c,e) and largely oligopolistic in market structure. The private sector in general suffered from effects of aggregate demand contraction in the form of credit contraction and declining real wages (World Bank 1988d).

In the 1990s the country was still suffering from poor economic performance, social indicators, income distribution and institutions brought about by years of an elitist development strategy. Its population growth rate was one of the highest in the world being both a cause and an effect of poverty and there was an alarming percentage of the population infected with HIV. Soil erosion and deforestation had reached excessive levels with shortages of wood, water and productive land made worse by unresolved land access and ownership issues. The government faced the challenge of managing an open economy that is subject to intermittent droughts and exogenous shocks. With drought and democracy making the politics of food security even more pressing, the role of ADMARC and the government in food markets still needed to be clarified. The World Bank initially adopted a sophisticated approach to market liberalisation and the role of ADMARC:

Agricultural market liberalisation is not a simple matter for a number of reasons. It is not clear that liberalisation efforts in a few markets will lead to economic gains for all smallholder groups as long as there are rigidities, imperfections and failures in other markets. This is the well-known theory of the second best... Furthermore, liberalised markets are not synonymous with competitive markets, and a mere removal of restrictions will not necessarily lead to optimal or efficient outcomes, let alone equity and poverty reduction. (World Bank 1995, p.27)

Despite this initial caution, tensions rapidly emerged between the Bank and the government on the pace of market liberalisation and particularly the role of ADMARC. Heavy borrowing by ADMARC contributed to the government's inability to meet the public sector deficit target and credit ceiling target of the IMF's Extended Fund Facility and so causing suspension of the IMF programme in the country (Gulhati 1989). The Bank pushed for a complete government withdrawal from agricultural markets, advocating that ADMARC be commercialised and privatised and that food security be taken care of by a National Food Reserve Agency, a Trust formed to run the country's decentralised strategic grain reserve on a rule-based method of intervention.

The government was accused by many donors, particularly the Bank and IMF, of intervening in markets in a manner which crowded out private traders. The government for its part, supported by a few donors, argued that privatisation had been too rapid and that market liberalisation had been



promoted more with the objective of reducing fiscal deficit than promoting efficiency and competition. However, partly in response to the above mentioned policies and partly reflecting favourable weather as agriculture bounced back from the 1992 and 1994 droughts, there was a remarkable growth led by the smallholder sector. In 1995 and 1996 smallholder growth registered 43.6% and 41.0% respectively and the economy as a whole expanded by 14.3% and 10.9% (Table 4.6). Tobacco was the driving force in this growth and the major cash injection brought multiplier linkages to the rest of the non-farm rural economy.

<b>Table 4.6: Key Macroeconomic Indicators: 1993 -1999</b>							
	<b>1993</b>	<b>1994</b>	<b>1995</b>	<b>1996</b>	<b>1997</b>	<b>1998</b>	<b>1999</b>
Real GDP growth %							
(1994 factor cost)	4.9	-12.3	14.3	10.9	5.0	3.3	6.7
Agricultural growth %	31.3	-48.7	40.0	32.2	3.3	2.7	13.6
Small holder growth %	51.8	-47.4	43.6	41.0	0.9	7.7	17.0
Estate growth %	1.0	-51.8	30.3	9.6	11.2	-12.3	0.9
Manufacturing growth %	-9.5	10.5	5.5	-1.4	0.6	0.3	1.6
Price infaltion rate %	22.8	34.6	83.3	37.6	9.2	29.8	44.8
Govemment deficit % of GDP	-8.9	-16.2	-5.1	-7.9	-9.1	-4.4	NA
Investments % of GDP	32.4	26.8	13.9	9.6	9.8	11.4	11.6
Tobacco sales MT'000	133.2	97.6	129.6	128.5	158.1	134.4	110.0
Average exchange rate MK: \$US	4.4	13.5	23.3	22.2	16.6	31.9	44.1
Interest rate %							
(Reserve Bank Discount Rate)	25.0	40.0	46.0	42.0	25.0	32.0	47.0
N/A = data not available							
Source: Reserve Bank of Malawi, various years							

During the 1990s, inflation rose from 11.5% in 1990 to 83.3% in 1995. Prudent policies introduced in 1995 reduced the inflation to 37.6% in 1996 and to 9.2% in 1997. However, the depreciation of the MK in 1998, led to the rise of inflation to 29.8% and 44.8% in 1998 and 1999 respectively (Table 4.6). High fiscal deficits between 1994 and 1999 necessitated more government borrowing which in turn led to high interest rates. Lending interest rates moved from 40% to 47% during that period. Manufacturing growth declined from 10.5% in 1994 to -1.4% in 1996. Contributing factors included poor macroeconomic environment and lack of fiscal incentives. High interest rates act as a disincentive to investment and therefore retard economic growth and worsen poverty as the poor fail to raise credit resources to participate in production.

The major challenges for the Malawi commodity trade have been price competitiveness, quality and production levels. Malawi prices have been higher at a number of markets particularly, which



rendered Malawi's exports unattractive. Production levels remained low and Malawi failed to satisfy export requirements even for readily available markets. Quality has also been very critical with regards to physical appearance of commodities and in some cases chemical content. There has also been poor flow of market information to small exporters particularly those in rural areas. The country has not benefited from international and bilateral trade agreements either. The COMESA agreement has let down some businesses in Malawi and so has trading with Zimbabwe. At the writing of this report, efforts were being made to iron out the 'misunderstandings'. Malawi was also eligible for another initiative, Africa Growth Opportunity Act, by the American government, to provide SSA countries with an opportunity to trade with the United States (US) in selected items. However, competition from more advantaged SSA countries has been too stiff for Malawi hence missing out on the chance to expand on the market it supplies.

#### **4.5.1.1 Policy impact on the Smallholder sector**

As discussed in the policy reform sections, several measures were propagated by the World Bank and the IMF to improve the performance of the smallholder farmer sector, which had a negative average annual growth rate of -3.9% between 1979 and 1981. The most important policy actions impacting on this sector were: a price reform policy, liberalisation of the marketing of crops, the restructuring of ADMARC and a removal of input subsidies such as that on fertiliser. The price reforms introduced in the early 1980s aimed to increase smallholder income and to diversify export crops. ADMARC's producer prices of smallholder crops were raised several times during the 1980s and the early 1990s (Sijm 1990). Higher prices made it attractive for smallholders to sell food and other crops rather than keeping them for home consumption such that by the end of a season most smallholders became buyers of food and had to buy maize for which they had no money. The price reform policy overlooked the structural problems within the stagnating smallholder sector. The sale of maize increased but the production of maize did not increase sufficiently to feed the increasing population. There was no increase in the export of smallholder crops, another important aim of the price reform policy, until 1990 when, as part of the ASAC, the government decided to allow smallholders to grow burley tobacco. As discussed in earlier sections, this resulted in an increase in the export of smallholder crops but because Malawi is one of the world's largest producers of burley tobacco, the increase in output led to a decline in prices on the world market and thus to a decline in returns (Economist Intelligence Unit 1995).

Overall, the SAP measures taken to improve the performance of the smallholder sector were not successful. The production of the sector increased slightly but at a lower rate than the growth in population leading to a decline in growth rates per capita and a decline in maize and total food



production per capita (Government of Malawi/UNDP 1993). The liberalisation of trade in crops caused price increases which negatively affected the majority of smallholder households as they sold their maize at a relatively low price only to buy it back at a much higher price later on.

#### **4.5.1.2 Policy impact on the Estate sector**

During the period of structural adjustment very few measures were aimed at improving the performance of the estate sector and the excessive reliance on only three export crops remained. The World Bank considered that many managerial problems had to be overcome before new export crops could be introduced. These managerial and other structural problems were, however, not addressed and very little changed in the policies towards the estate sector (Harrigan 1991). Despite the absence of measures to improve the functioning of the estate sector, it grew by 127 per cent between 1979 and 1993 and by 40 per cent per capita, a much greater increase in sectoral GDP than the smallholder sector which grew by 33 per cent in total and which had negative per capita growth rates over the period (Government of Malawi/UNDP 1993).

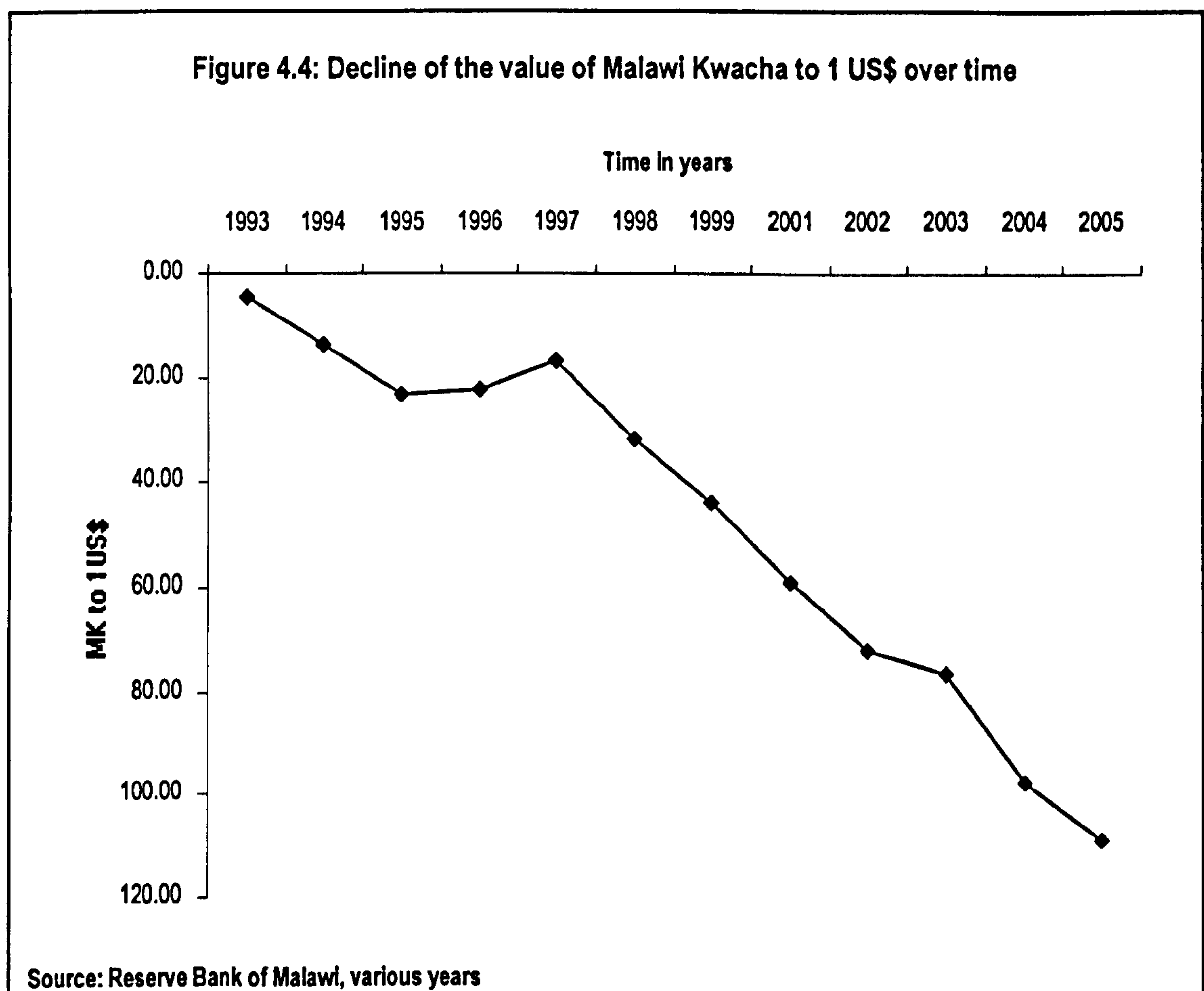
#### **4.5.1.3 Policy impact on the External sector**

Trade policy reform, namely dismantling controls over imports and foreign exchange allocation and a rationalisation and general lowering of import tariffs has been a central feature of the economic reform programme (World Bank 1994). As discussed in previous sections, Malawi's significant import liberalisation took place at the end of the 1980s with the removal of administrative controls in the form of prior foreign exchange approval under the World Bank's ITPAC. In parallel with the policy enhancing the availability of foreign exchange and liberalising its allocation, Malawi was advised to devalue its currency as its exchange rate was considered to be overvalued and the currency has since been substantially devalued over the years. The MK was devalued by 1600% from 4.4 MK to 76.7 MK to 1 US\$ between 1993 and 2003 (Figure 4.4).

There are potential side effects of currency devaluation on inflation, employment, output growth, real wages and income distribution (Cooper 1971). However, a distinction needs to be made between nominal and real exchange rate (RER). The nominal exchange rate is a monetary concept that measures the relative price of two moneys, like MK to US\$, whereas the RER measures the relative price of two goods and is defined as the relative price of tradables with respect to non-tradables. RER is a good proxy of a country's international competitiveness, as it corrects the nominal rate for inflation. In theory, nominal devaluation will affect an economy through three main channels. Firstly it has an expenditure-reducing effect whereby domestic prices rise and real value



of all assets (including the domestic money) is reduced. Expenditure on goods, including tradables, will reduce and so will the trade deficit. Then there is the expenditure-switching effect whereby the relative price of tradables to non-tradables is altered. Expenditure switches away from tradables, and production towards them. Depending on which of these effects dominate, demand for domestic home goods will either rise or fall. Thirdly, nominal devaluation may boost the domestic currency price of imported intermediate inputs, pushing up the supply schedules for final goods (Edwards 1986b). Overall, nominal devaluation is meant to increase the domestic price of all tradable goods, services and assets.



Nominal devaluations, which raise the local currency's price of a \$, cause the real rate to depreciate, at least initially. If domestic prices then increase more rapidly than world prices, however, the local currency appreciates in real terms. And this is what happened in Malawi from the late 1980s when inflation brought a significant appreciation of the real exchange rate and a loss of external competitiveness. Appreciation of the RER reduces profitability of any firm producing exports or import-competing goods since the domestic cost of producing tradable goods increases. The aim is to keep the exchange rate at a level that makes it profitable to invest in exports, and to maintain the RER at a steady level over long periods (Willet 1986). This can be achieved through



changing of the nominal rate, keeping budget deficit under control and restriction of money creation to restrain domestic price inflation. Overvalued RER hurts exports and if maintained for long periods, it has been argued that it can even wipe out the agricultural infrastructure and also generate capital flight (Pfeffermann 1985). Nominal devaluation will boost the prices of imported inputs and consequently the cost of producing domestic goods. Over time it will result in a large increase in the RER. Then as prices of imported goods react to the nominal devaluation, the effect on the RER will be partially eroded. The aim is to produce a real depreciation. Therefore, although Malawi may have substantially devalued its currency over the years, it could be for the reason that in real terms, the exchange rate was still overvalued and may even have been more overvalued than before.

Nevertheless, a weaker currency is likely to cause a higher balance of trade. It tends to increase price paid for foreign goods and hence reduce demand for foreign goods. But it is necessary to devalue the nominal exchange rate periodically to maintain exporters' incentives. However, despite the nominal devaluations, exporting has not improved in Malawi. Inadequate export revenues and foreign investment have resulted in shortage of foreign exchange to finance imports needed to achieve growth and other development targets. When a business requires imports, such as capital equipment or raw materials, it reduces foreign exchange available to other businesses. If it yields additional foreign exchange by exporting its output, it benefits other businesses by providing more foreign purchasing power and if there are fewer businesses exporting it means less foreign exchange as the situation has been Malawi.

Malawi has been experiencing persistent BoP deficit over the years and a deficit in a country's BoP suggests that a country is spending a greater amount of funds on foreign products than it is receiving from exports to foreign countries; and because it is selling its currency (to buy foreign goods) in greater volume than the foreign demand for the currency, the value of its currency is decreased. However, the argument, by the World Bank, is that the decrease in value should encourage more foreign demand for its goods and hence increase exports in the long-run. With the rise of exports, there would be an improvement in the current account of a country's balance of payments and hence international reserves would rise and the exchange rate would soon appreciate (World Bank 1984).

#### **4.5.1.4 Policy impact on the Industrial/Manufacturing sector**

The importance of agricultural sector for the livelihood of most Malawians and the little importance attached to other economic sectors by the Malawi government often led to the neglect of attention



for the industrial and service sectors. And as seen earlier on, adjustment policy reforms relating to industrial sector were launched in 1988, well after the adjustment reforms in 1981. Furthermore, substantial trade policy reforms took place only since the mid-1990s, hence it is not possible to be as definite about the impact of the reforms on industry as it is with the impact on the agricultural sector.

The restructuring of the Press Corporation was one of the conditions of the second SAL, and the company became Press Group Limited (PGL) with the introduction of new guidelines concerning investments, price policy and savings to ensure that it operated on a commercial basis. By 1984, the restructuring of PGL was virtually completed. However, it was still difficult for common Malawians to establish a factory or other industrial enterprise. The number of establishments remained small and in 1988 only 407 were registered. The 1991 government budget statement attempted to break down the monopoly of the PGL and other large companies through a complete liberalisation of the investment environment in order to encourage Malawian entrepreneurs to participate in this sector (Economist Intelligence Unit 1995, Harrigan 1991a, Kalua 1992).

Price liberalisation of industrial products started in 1983 when 23 goods were decontrolled followed by 8 more in 1984 and 20 others in 1985 (Gulhati 1989). The government only retained control over petroleum products, fertilisers and sugar. This policy made it possible for firms to increase their prices in response to increased costs but contributed to high inflation and increased the cost of living for wage earners significantly, because salaries were not adjusted (Chipeta 1993). With the removal of exchange control procedures most inputs for industry were made more easily available and this increased the efficiency of the industrial sector. According to Chipeta (1993: 114), 'industry is reported to be operating at 50-60 per cent of capacity up from 20-30 per cent before trade liberalisation'. However, in 1991 a foreign exchange control system was re-instated because of a scarcity of reserves and the procurement of imported inputs became more difficult (Parker et al. 1995).

Despite the new policies targeting at the development of the industrial sector of the economy, the sector, which is still domestic-market-oriented, has not developed owing to low purchasing power of Malawians, lack of backward and forward linkages between industries, foreign competition and absence of a capital goods sector. Only 3% of manufactured goods were exported in the late 1980s (Sahn et al. 1990), accounting for only 6% of total exports during the 1980s and early 1990s (UNCTAD 1991, UNIDO 1987). A survey by Frischtak (1990) revealed that operational constraints impeding industrial response to adjustment included working capital finance, seasonality of



demand, high transportation and raw materials costs, and regulatory limits on location. Effects of the changes could, however, still have been working themselves out at the time of this study, but on the whole the Malawi industrial sector's performance in the 1990s was below expectations despite major reforms.

#### **4.5.1.5 Policy impact on SMEs**

The macroeconomic reforms had sought to stabilise Malawi's economy and increase competition in the domestic market, especially for import-competing producers. Measures which had direct implications for SMEs included devaluation of exchange rate to stimulate exports, price deregulation of industrial products to stimulate manufacturing investment, privatisation of state-owned enterprises and removal of industrial licensing requirements and reductions in tariffs. In principle, these reforms would benefit the SMEs in several ways: macroeconomic stability would improve business planning and investment by reducing uncertainty; increased competition would favour the most flexible existing firms and efficient new firms that enter in response to changing incentives.

In practice, however, the impact of SAPs was mixed, as most SMEs were ill-prepared to face increasing competition. Increased competition from low-cost imports squeezed out business profits and it is without doubt that most SMEs faced a much more competitive environment after structural adjustment. According to a study on small enterprises in five African countries, 70% of the sampled small scale enterprises in Malawi reported facing increased competition (Parker et al 1995). The increased competition was expected to force SMEs to make adjustment in order to survive, which did not happen for most. However there was a substantial amount of new entry into the sector, as a result of the free trade policy and political reforms (Parker et al 1995). By liberalising imports and reducing government control over resources, the government improved access of the private sector to inputs. However, Parker et al's study revealed that although import liberalisation in Malawi made imports more available to SMEs by removing previously restrictive licensing policies, currency devaluation raised the cost of imported inputs, favouring a shift to domestic products while a drop in real wages eroded domestic demand. It was also reported that 68% purchased new equipment, 50% changed product mix, 50% applied for a loan and 26% increased imported input use, as a result of the reform measures (Parker et al 1995).

Output for SMEs increased substantially in the period in which the country underwent deregulation in the rural economy and undertook significant trade policy and political reforms, which is 1995 as



most adjustment policies affecting SMEs were implemented during that time. There was a decline in output by 2.8% between 1990 and 1994 which could also be explained by droughts of 1992 and 1994 which reduced demand for goods. However, data from two small business enterprise surveys (Malawi Government 1994, 2000) showed that output grew by 332% between 1994 and 1998. The data also showed that value-added of SMEs increased by 60% per annum between those two survey periods. And this could be explained largely by the increase in number of SMEs in Malawi following liberalisation that ensued in the period after 1994. Trade policy reforms and deregulation of the economy, therefore, did not impede the growth of output of small-scale enterprise sector and may have helped it by promoting imports of intermediate goods and raw materials.

A major consequence of the devaluation of the national currency is the change in price of imports and exports. Imported goods become relatively more expensive and exported goods become relatively cheaper. Small enterprises that depend on imported inputs and raw materials have been adversely affected (Bagachwa 1993). In the Malawi case liberalisation has had a stronger effect than devaluation of national currency and led to an increase in the import of competing consumer goods. The availability of cheap goods is often caused by the dumping of these goods on the world market by large-scale producers in Asia or Western countries. Products are sold at a very low price and small local producers are unable to compete on price.

Trade policy, privatisation of parastatal and government macroeconomic policy are of relevance here because they can affect the prospects for private initiative and small and micro enterprise growth. Before implementation of SAP, controls were widespread and vast majority of firms produced under conditions of no foreign or domestic competition, and foreign exchange rationing severely constrained access to imports of machinery, spare parts and raw materials. Belief is that liberalisation in general, and trade reform in particular, should have a strong positive impact on productivity. And indeed it has been reported that in Malawi most firms increased productivity after economic liberalisation (Parker et al. 1995). However, regarding effects of opening up to international trade, Harrison and Revenga (1995) argued that economists have not reached a consensus on the relationship between liberal trade policies and productivity.

In general, the reduction in the role of the state led to a strong increase in the number of people involved in informal businesses (Callaghy and Ravenhill 1994, Cornia et al. 1994, Nabuguzi 1994, Shaw 1992). It is without doubt that the structural reforms and political changes, in Malawi, revised the regulatory environment that previously made it difficult for potential investors to start-up a



business. As a result it is easy for Malawians to enter into the SME sector, but to sustain the enterprise it is another matter.

#### **4.6 Malawi: Beyond SAPs**

This section gives an update on policy changes in Malawi in recent years. It should be noted that some of the events do overlap between the SAP years and the years after 2000. Indicators and the discussion presented are descriptive rather than analytical and have been included to provide an update on the current economic situation and changes in policy, which have taken place over the past five years both nationally and internationally.

Linked in to poverty reduction initiative discussed in Chapter Three, the IMF established a new type of lending to low-income countries, called the Poverty Reduction and Growth Facility (PRGF) in 1999. This facility is meant to be IMF's low-interest lending facility for low-income countries underpinned by each country's own poverty reduction strategies. Malawi is one of the countries, which subscribed to the PRGF through its interim PRSP, which was first launched in April 2002. The aim of the strategy was to reduce poverty through economic growth and empowerment of the poor. The first review of the initiative was completed in October 2003 and reported unsatisfactory implementation, rendering Malawi's economic performance under the interim PRGF arrangement disappointing. Macroeconomic developments during 2002 were, as noted in the progress report, below expectations. Real GDP was less than 2% in 2002. On the other hand inflation decreased from 30% in 2000 to less than 10% in June 2003. However, high interest rates continued to constrain private sector development (IMF 2004a).

Although the arrangement was extended to December 2004, the second review could not be completed due to fiscal slippages rendering the arrangement off-track and also that the PRGF had been off-track since 2001. The IMF blamed all these problems and poor economic performance on weak governance and programme implementation on unstable macroeconomic situation, which was characterised by large fiscal slippages, unsustainable domestic debt spiral and low domestic investment. Stabilisation was not attained and the PRGF arrangement was allowed to lapse after completing only one review. This led to suspension of external budgetary assistance and to increased resource to domestic borrowing to finance large budget deficits. The suspension of budgetary assistance by donors resulted in increased domestic borrowing, which contributed to high interest rates and a rise in domestic debt (Malawi Government 2004). A new government elected in July 2004 requested a twelve-month Staff Monitored Programme (SMP) from the IMF in



order to establish a track record that could lead to the re-establishment of the PRGF arrangement. It was agreed that the country be put under SMP whilst working towards a new PRSP.

There has not been much change over the past five years with regards to the economic structure. The share in industry actually declined in relative importance and agriculture continues to account for 36% of GDP with an estimated 90% of workers still depending on agriculture as a major source of income. Despite higher tobacco production, export performance did not improve, due to temporary processing difficulties. The import bill rose in response to stronger domestic demand and higher oil prices. There is every indication that the Malawi economy is still in a poverty trap as over half the population remains below the official poverty line (Malawi Government 2004). Also, the population of 11 million people puts severe pressure on land as arable land is very limited, and is intensified by population growth of 3.2% per annum accentuating the need for programmes to foster rapid development of off-farm employment activities. The demographic problems are compounded by the high prevalence of HIV/AIDS, which has a devastating impact on the prime-age labour force.

Performance in attaining the macroeconomic stability has been below expectations and inflation rate rose from 9.6% in 2003 to 19.9% in 2004 (Table 4.7) Overall growth performance has been very poor, signalling fundamental problems with the enabling environment for private sector development. However, whilst performing poorly between 2000 and 2002 (GDP declining to as low as -4.1% in 2001) growth exceeded 4% in 2003 and 2004. Inequality of income is also still a serious problem with just 4.9% of total household income accruing to the poorest 20% (Malawi Government 2004).

**Table 4.7: Recent Macroeconomic Indicators: 2000 - 2004**

	2000	2001	2002	2003	2004
Real GDP growth %	2.0	-4.1	1.8	4.4	4.6
Exports (as % share of GDP)	23.1	25.0	21.9	27.5	27.3
Imports (as % share of GDP)	35.4	36.8	38.5	40.6	38.2
Balance of Payments (before debt relief) MK bn	-7.1	-6.3	5.9	-5.4	-6.6
Manufacturing growth %	-2.5	-14.2	-0.1	2.2	3.9
Real interest rate %	53.6	24.7	28.1	39.3	N/A
Debt Service as % share of GDP	2.7	3.9	4.5	9.5	4.7
Government Revenue MK bn	16.0	21.5	24.7	24.7	24.9
Price Inflation rate %	29.6	27.2	14.8	9.6	19.9
Exchange Rate (Malawi Kwacha = \$1)	59.5	72.2	76.7	96.8	108.6

N/A = data not available

Source: Reserve Bank of Malawi: Finance and Economic Review, various years



Malawi owes US\$2.9 billion, most of it being to the WB. Debt service payments between 1996 and 2001 were averaging US\$93 million per year. It has been argued that even after HIPC debt relief, Malawi would still have unsustainable debts, although the initiative has helped ease an earlier debt overhang (IMF 2005b). Performance under SMP was believed to be satisfactory with the authorities committed to macroeconomic stability such that approval of a three-year PRGF arrangement and additional HIPC assistance was recommended. The IMF executive board approved a three-year PRGF on 5 August 2005 to provide US\$55 million to support the implementation of Malawi's economic reform programme. The first review conducted in September 2005, reported satisfactory implementation. It was hoped that under SMP, the HIPC completion point would be reached by mid-2006, if outstanding triggers were implemented (IMF 2005b).

As for the business environment, corruption has been getting worse over the past five years. However, according to an IMF report, the Malawi government has recently taken steps to implement a zero-tolerance policy for corruption and anticorruption efforts were also moving ahead with some former government officials arrested and being investigated (IMF 2005b). This is welcome news for growth prospects if it proves to be a serious commitment. Those businesses obtaining loans, cost was still very high as real interest rate on bank loans were still on the rise. The prohibitive cost of borrowing is related to government's large demand for credit to finance the budget deficit, which crowds out financing for the private sector. Also, there is a highly concentrated financial system that allows banks to charge what the market will bear which indicates that the financial system is still underdeveloped and is proving to be a bottleneck for growth. Problems with electricity supply are still creating a competitive disadvantage for local businesses. The government completed an extensive review of tax policies and administration in early 2005 with an overall objective of a fair and competitive tax regime with efficient administration. Starting with the 2005/06 budget, some tax rates were to be reduced and the base broadened (IMF 2005a).

The Malawi government developed a new programme for 2005 to 2008, which aims to promote growth by fostering a financially sound and stable macroeconomic environment and by undertaking structural measures to improve economic efficiency. Policies would be guided by the objectives and strategies which were set out in the Malawi PRSP (2003). The government was also planning to focus on international barriers to trade by repairing and building rural roads and improving international rail links. These improvements, to public infrastructure, were intended to address the high cost of doing business in Malawi. Also included in the growth strategy is the initiative to bolster



non-tobacco exports. The government has also eliminated all quantitative restrictions on imports and the trade agreement with Zimbabwe was revised and signed in March 2005 (Malawi Government 2005a).

#### **4.7 Summary**

Malawi experienced strong economic growth in the period between 1964 and 1974. From 1979 onwards, however, the country faced economic difficulties leading to income contraction and a decline in the purchasing power of a large sector of the population. The Government regarded the estate sector as the engine of growth, able to generate economic development and increase living standards for all Malawians through creation of employment and generation of foreign exchange through the export of crops. It is apparent that this strategy and the large-scale industrialisation process adopted by the Malawi government since independence did not bring about expected economic growth. 1979 to 1981 saw worsening of the economic performance and hence the Malawi government sought advice and help from the IMF and WB, and help was given in the name of Structural Adjustment Programme.

Between 1981 and 1994, Malawi implemented six structural adjustment programmes (SALs I to III, ITPAC, ASAC, ESAF) supported by the IMF and WB. Malawi's SAPs consisted of three major elements: measures to establish fiscal discipline, such as comprehensive tax reform, a reduction in government expenditure, improved budgetary planning; agricultural reforms such as an increase in producer prices, the expansion of the role of small private farmers, and greater incentives for more efficient large-scale production and; trade liberalisation such as the phasing out of import and export taxes and exchange controls, a rationalisation of the tariff structure, and a devaluation of the MK. The SAPs were meant to rectify inappropriate past policies that were believed to be hampering economic performance. To offer the increasing number of Malawians the possibility of generating income through the establishment of an industrial enterprise and to stimulate indigenous entrepreneurship required measures to change the structure of the industrial sector which was done through the ITPAC. As a result of the SAP and political reform policies, there are thousands of enterprising people in Malawi, but very little vibrant private enterprise.

Throughout the 1990s the Malawi economy remained very vulnerable to external shocks, resulting in considerable fluctuations in GDP growth. Throughout the 1990s and up to now the Malawi economic growth indicator has been fluctuating. The structure of exports remained rigid within the same traditional exports of tobacco, tea and sugar dominating. Malawi has a long way to go to reach the MDGs and cannot do so without external aid. In order to implement its poverty reduction



strategy and to boost spending further on infrastructure and the social sectors, it will have to rely on a significant increase in external aid flows over the medium-term. The main framework for donor support is its PRSP, which was re-established in 2005. Although Malawi is now a relatively open economy, data reveal serious problems in the external sector. The country is still experiencing very low export growth, highly concentrated export earnings, high dependency on foreign aid, very low inflows of foreign investment and low levels of foreign exchange reserves (Reserve Bank of Malawi 2005).



## Chapter Five

### Small-Scale Enterprise Development in Malawi

#### 5.1 Introduction

Many non-agricultural activities require little investment or schooling, and as a result any individual can start-up a small business and generate some money. This accessibility has made non-agricultural activities popular among regional planners and non-governmental organisations as they see these activities as a panacea for all sorts of problems experienced in developing countries, notably poverty and unemployment. However, as a result of globalisation and SAPs, small-scale domestic enterprises of SSA have been exposed to competition before they are able to increase efficiency and competitiveness, and it seems evident that liberalisation is associated with increased competition from imports (Grenier et al. 2000). Before analysing and discussing the impact of SAPs and globalisation in the following chapters, the micro and small sector enterprise development in Malawi is discussed and presented in this chapter in order to provide background information and relevant basic statistics for the sector.

The rest of the chapter is organised as follows: the second section gives definitions of fundamental terms used in this and subsequent chapters; the third section discusses the role and characteristics of micro and small enterprises and impact of structural adjustment on the SME activities; section four summarises. The data referenced in this chapter is from a survey which was carried out on micro and small enterprises in Malawi in the year 2000.

#### 5.2 Definitions

It is thought important to begin by defining what entrepreneurship means before discussing enterprises. Some scholars have defined *entrepreneurship* as a process of creating value by bringing together a unique set of resources to exploit an opportunity (Maasdorp 1998, van Vuuren 1983). In a strict sense, entrepreneurship has three key underlying dimensions: innovativeness, calculated risk-taking and pro-activeness (Morris and Sexton, 1996). As such, entrepreneurship is a variable phenomenon, with different degrees at any point in time. The vital force behind the transformation of certain East European economies into successful free enterprise societies has been due to entrepreneurship, while some of the so-called East Asian economic miracle has also been largely attributed to the establishment and growth of an enterprise culture. It is assumed that because of high illiteracy and unemployment rates in SSA, people do not have the entrepreneurial qualities and traits described by the entrepreneurship scholars. As such, this study did not look for



such traits when selecting the target study population. The researcher took the view that 'entrepreneurship' was any income generating activity, either formal or informal.

After establishing what entrepreneurship is in this research, enterprises are defined as businesses engaged in manufacturing, processing, assembly or repair, servicing and trading activities and agricultural enterprises marketing their products. The term 'industries' has been used to cover manufacturing, processing of primary products and related repair services as defined by Chuta and Sethuraman (1984). Small-scale enterprises are usually defined as enterprises employing up to 50 people. A further sub-division is also made into small-scale enterprises (10-50 workers) and micro-enterprises with less than 10 workers (Liedholm 1990, Livingstone 1991, Parker and Torres 1993, UNIDO 1991). Some authors define micro-enterprises as businesses employing fewer than 5 workers (Parker et al. 1995, UNDP et al. 1988). Some authors maintain that these small enterprises are part of the informal sector and thus characterised by their ease of entry, their competitiveness, their reliance on indigenous resources, their low technical level and by the fact that they do not adhere to regulation concerning wages, taxes and permits (Grey-Johnson 1992, Livingstone 1991). The Government of Malawi developed an official definition of enterprise sizes in 1992, which describes enterprises on the basis of three parameters, namely capital investment, employment and turnover. The official definition is that 'micro' enterprises are those that have a capital investment of up to US\$1,000, employ 1-4 people and have turnover of up to US\$4,000. 'Small' enterprises are defined as those with a capital investment of up to US\$50,000, 5-20 employees and a turnover of up to US\$100,000. Firms with 21-100 employees are defined as 'medium' size whereas those with more than 100 employees are 'large' scale enterprises.

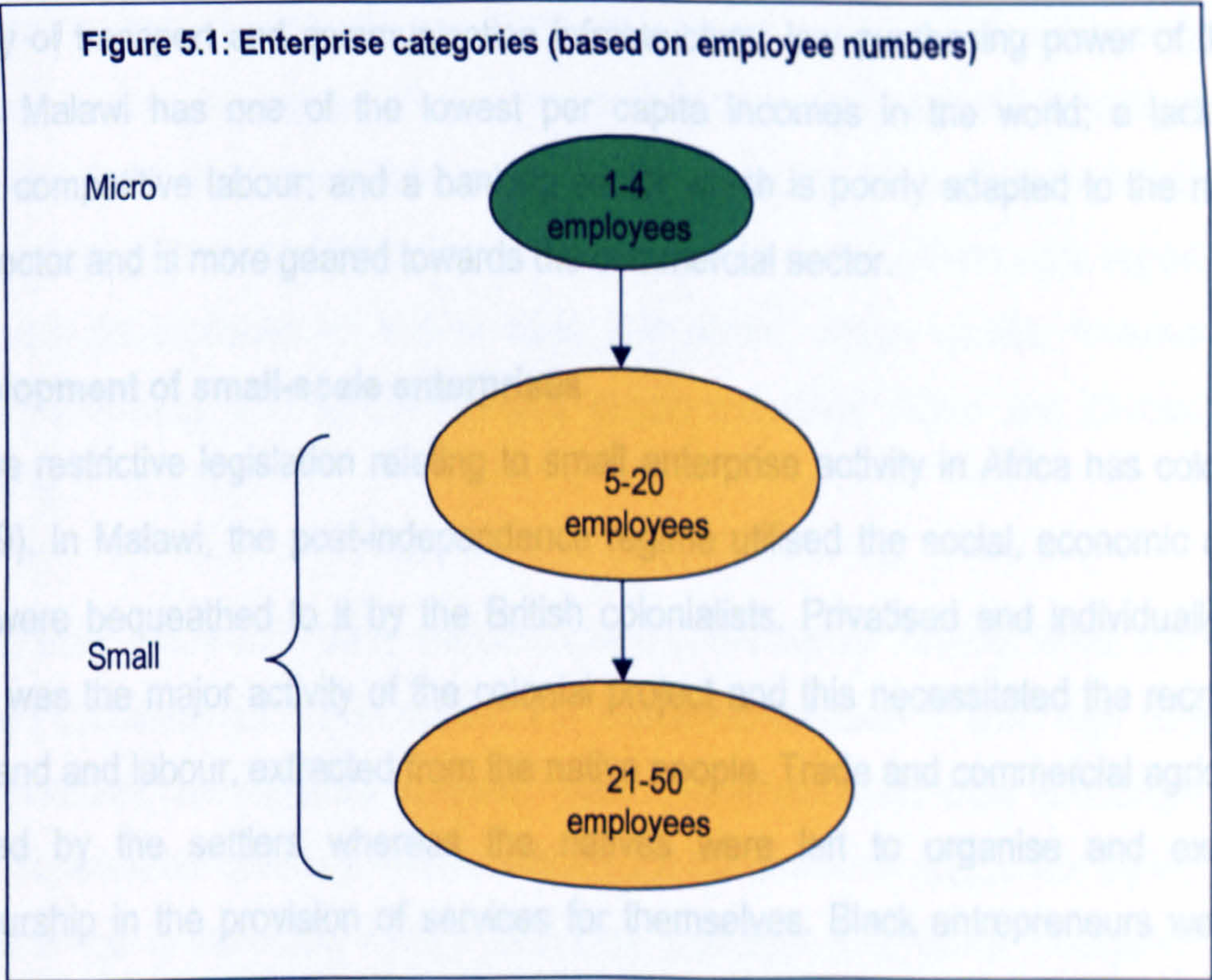
The following definition is used to describe small-scale enterprises, for Growth and Equity through Micro-enterprise Investments and Institutions (GEMINI) micro and small enterprise baseline surveys:

Business activities that employ 50 or fewer employees, inclusive of the proprietor(s). In addition, for crop-agricultural enterprises, the definition includes only those businesses that have sales of at least US\$ 100 per year (or relevant Malawi kwacha round figure). For all other businesses we include only businesses that market at least 50% of their production (Malawi National GEMINI 2000, Annex 2).

In this definition, a 'business' is considered an activity that sells 50% or more of its goods or services. 'Employees' are defined as working owners, paid workers, unpaid workers and trainees, both full and part time workers. The employment-based definition has been used by many related studies in southern Africa and has been found to be easily measurable, relatively inexpensive and not necessarily less reliable than the more complex definitions (Parker 1996). Within this



framework, the GEMINI study targeted businesses with 1-50 employees and classified them all as 'micro and small' enterprises. The GEMINI definition was adopted for this study and was used to refer to study units of this survey and for comparison purposes with previous and future baseline surveys in Malawi. The study units included independent firms, not forming part of a larger enterprise, having small market share and not influencing to any significant extent the price or total quantities of goods sold. As in the GEMINI survey, the terms 'small and micro enterprises' (SMEs) has been used throughout this study to refer to all enterprises with less than 50 employees, which is also further subdivided into three categories (basing on employee numbers) as laid out in Figure 5.1. It should be noted that although GEMINI survey analysis tables distinguished between the 5-20 and 21-50 categories, they were both still referred to as small enterprise categories.



Another important term which has been mentioned above and which is relevant to discussions in the following chapters is the 'informal' sector. The concept 'informal sector' originated from observation (in the early 1970s), that the modern sector (particularly manufacturing) was unable to absorb a growing surplus of manpower in developing countries (Levin 1994). Earning opportunities outside the formal sector had therefore to be found to ensure survival for the unemployed. Since then the term 'informal sector' evolved as a generic and practical term covering all survival efforts employed by the poor and the unemployed outside the formal sector and this is the definition adopted in this study.



### **5.3 The SME sector in Malawi**

Unlike the formal industrial sector, the SME sector (both formal and informal) occupies an important place in the Malawi economy, at least in terms of employment it provides. In urban areas, the majority of population depend on this sector for a living. The urban exodus caused by the droughts and the economic recession has created an influx of labour to the informal SME sector. This sector also absorbs the people dismissed from the 'deflated' public sector and civil servants on voluntary retirement. In addition to the constraints associated with variations in weather, the development of the SME sector in Malawi is slowed down by a number of structural obstacles which have a negative effect on productivity and the capacity of enterprises to be competitive in domestic and export markets. Among these constraints are: limited integration of the industrial structure which forces most enterprises operating in the modern industrial sector to import their raw materials; insufficiency of transport and communication infrastructure; low purchasing power of the national market, as Malawi has one of the lowest per capita incomes in the world; a lack of skilled, productive, competitive labour; and a banking sector which is poorly adapted to the needs of the industrial sector and is more geared towards the commercial sector.

#### **5.3.1 Development of small-scale enterprises**

Much of the restrictive legislation relating to small enterprise activity in Africa has colonial origins (Tripp 1989). In Malawi, the post-independence regime utilised the social, economic and political tools that were bequeathed to it by the British colonialists. Privatised and individually organised agriculture was the major activity of the colonial project and this necessitated the recruitment and control of land and labour, extracted from the native people. Trade and commercial agriculture were monopolised by the settlers whereas the natives were left to organise and exercise their entrepreneurship in the provision of services for themselves. Black entrepreneurs were active in retail trade, transport and small crafts and commodity production for the poorer populations in those urban and rural areas designated for blacks. Colonial policies undermined household and village industries and as a result indigenous artisans could not benefit from the growth of urban demand in order to grow in number or to make a transition from purely household-based production towards small urban workshops.

The suppression of retail trade meant that small enterprise rural/urban trade linkages did not develop. Since the population in the townships was meant to provide labour services to the colonial economy, independent economic activity as well as situations conducive to such activities was heavily regulated. It must also be noted that the state was an important agency for organising enterprises through the granting of inputs, credit and other support to colonial ventures in the public



and private sectors and this was instrumental in marginalising the native populations. The infrastructure was underdeveloped, and little industrial development had taken place. The only resources available in abundance were fertile land and a cheap labour force. The industrial sector consisted of tea processing, grading and packing of tobacco and ginning of cotton, enterprises owned mainly by Europeans, with distribution and transport businesses largely owned by Asians (Burdette 1990).

After independence, the Malawi government encouraged private investors to invest in industry by offering improved industrial sites liberal tax regulations, financial incentives for capital investments, tight regulations of the labour market and tariff barriers against Rhodesian goods (Burdette 1990). This policy seemed to work and the importation of consumer goods declined from 42% of total imports in 1964 to 21% in 1973 (Thomas 1975). The growth rate of the manufacturing sector as a whole was impressive, averaging 16% per year from 1964 to 1973 and 9% annually from 1970 to 1980. However, these high growth rates are somewhat deceptive because of the initial small size of the industrial sector (Burdette 1990). The main contributors to this growth were import-substituting industries such as producers of bottled beer, soft drinks, cheap textiles, footwear and basic agricultural implements, and agro-processing export industries (Kydd and Christiansen 1982, Thomas 1975).

Between the early 1980s and 1990s, the devaluation of the Malawi *kwacha*, which occurred twice a year, caused difficulties for import-substitution industries because of their high dependence on imports of industrial raw materials (Chipeta 1993). These industries were confronted with higher prices and experienced severe problems throughout the structural adjustment period and growth was in decline due to increasing foreign exchange shortages (Economist Intelligence Unit 1995). Throughout this period the production of goods for the domestic market remained much more important than the export of manufactured goods (Sahn et al 1990). The limited importance of the manufacturing sector was caused by the small domestic market for manufactured goods adversely affected by the slow growth in agricultural incomes. Other barriers were limited human capital and transport bottlenecks which increased costs of both exports and imports of goods and equipment. Furthermore, the adverse world economic climate, which affected exports through protectionism and increasing competition and affected import-substitution industries because of the high costs of inputs also negatively, influenced developments within the manufacturing sector (Chipeta 1993, Gulhati 1989, Pryor 1990).



Several studies have been conducted in Malawi since the early 1980s to establish the magnitude of what is often called the small enterprise sector (Daniels and Ngwira 1993, Ettema 1983, Webster and Mooney 1989). The studies have shown that the size of this sector has increased enormously. A study by Mead in 1994 estimated that, between 1981 and 1990, 56% of the increase in the total labour force was absorbed by the small enterprise sector (Mead 1994). However, as a result of past policy neglect, very little was known about the character, range of economic activities and extent of the small-scale enterprise sector in Malawi up until the results of two SME baseline surveys commissioned by the government in 1992 and 2000. Key findings of the 2000 GEMINI survey are presented in the following section.

### **5.3.2 The Role and Distribution of SMEs in Malawi**

Micro and Small enterprises are recognised as an important source of employment and income to many people at the bottom of the ladder. However, SMEs are rarely evident and often quite difficult to identify and count let alone identify their dynamics. This problem is compounded in Malawi, where 85% of the population resides in rural areas. This means SMEs are likely to be purely informal in nature and consequently more difficult to identify. As part of the Malawi government's efforts to support the SME sector, a baseline survey (GEMINI survey) of SMEs was jointly commissioned by the government and DfID to gain insight into the distribution of SMEs in the country by sector, size and ownership; business characteristics and economic performance; actual contribution to employment and incomes; key problems and effect of current business support services. Countrywide surveys conducted in 1992 and 2000 offered an opportunity to learn how this important sector changed over the SAP period of the 1990s. Both surveys employed the same general methodology, which has come to be known as the GEMINI survey technique.

The Malawi 2000 Micro and Small Enterprise (MSE) baseline survey was conducted during the period between October and December 2000 and covered about 747,000 formal and informal enterprises and firms with up to 50 employees, operating in the most representative sub-sectors of activity of the Malawi industrial structure. A questionnaire for GEMINI-style similar surveys was used and the sample was determined by randomly selecting census enumeration areas from which all micro and small enterprises were surveyed. Two enterprise sizes were defined according to the size of the permanent staff and selling 50% of produce: micro-enterprises (micro) with a permanent staff of less than 5 persons; and small enterprises with a permanent staff of 5 to 50 persons. The survey results showed that 70% of the SMEs are based in rural areas, 17% in the four cities of the country, 8.8% in small towns and 4.3% along the lakeshore area.



Tables 5.1, 5.2 and Figure 5.2 show the characteristics of the sample by size of enterprise, gender of owner and employment offered by each of the sub-sectors and by sector of activity . The SMEs were split between the traditional off-farm employment activities (manufacturing, construction, commerce and trade, transport and services) accounting for 74.6%, and agriculture, mining and natural resource sectors, which accounted for 25.4% of the enterprises. Out of total enterprises surveyed, 91.3% were micro with 1-4 employees, 8.5% had 5-20 employees and only 0.2% had 21-50 employees. All of the enterprises in forestry were micro size, and none of the enterprises in livestock, mining, manufacturing, construction, transport and services had more than 20 employees (Table 5.1).

**Table 5.1: Characteristics of sampled enterprises by size**

Sub-sector of Activity	AGRICULTURE, MINING AND NATURAL RESOURCES						OFF-FARM EMPLOYMENT ACTIVITIES				
	Total %	Crops	Live-stock	Forestry	Fishing	Mining	Manuf-acturing	Constr-uction	Commerce Trade and Hotels	Transport	Services
<b>Size:</b>											
1-4	91.3	70.5	70.9	100.0	62.1	86.4	97.2	78.9	96.8	92.9	93.5
5-20	8.5	29.1	29.1	0.0	37.5	13.6	2.6	21.1	3.1	7.1	6.5
21-50	0.2	0.4	0.0	0.0	0.4	0.0	0.0	0.0	0.2	0.0	0.0

Data Source: Malawi GEMINI MSE Survey 2000

As regards to enterprise ownership there was not much difference between percentages for females and males, 34% and 35% respectively (Table 5.2). Out of the female SME owners, most were in commerce, trade and hotels (46%) and in manufacturing (43%).

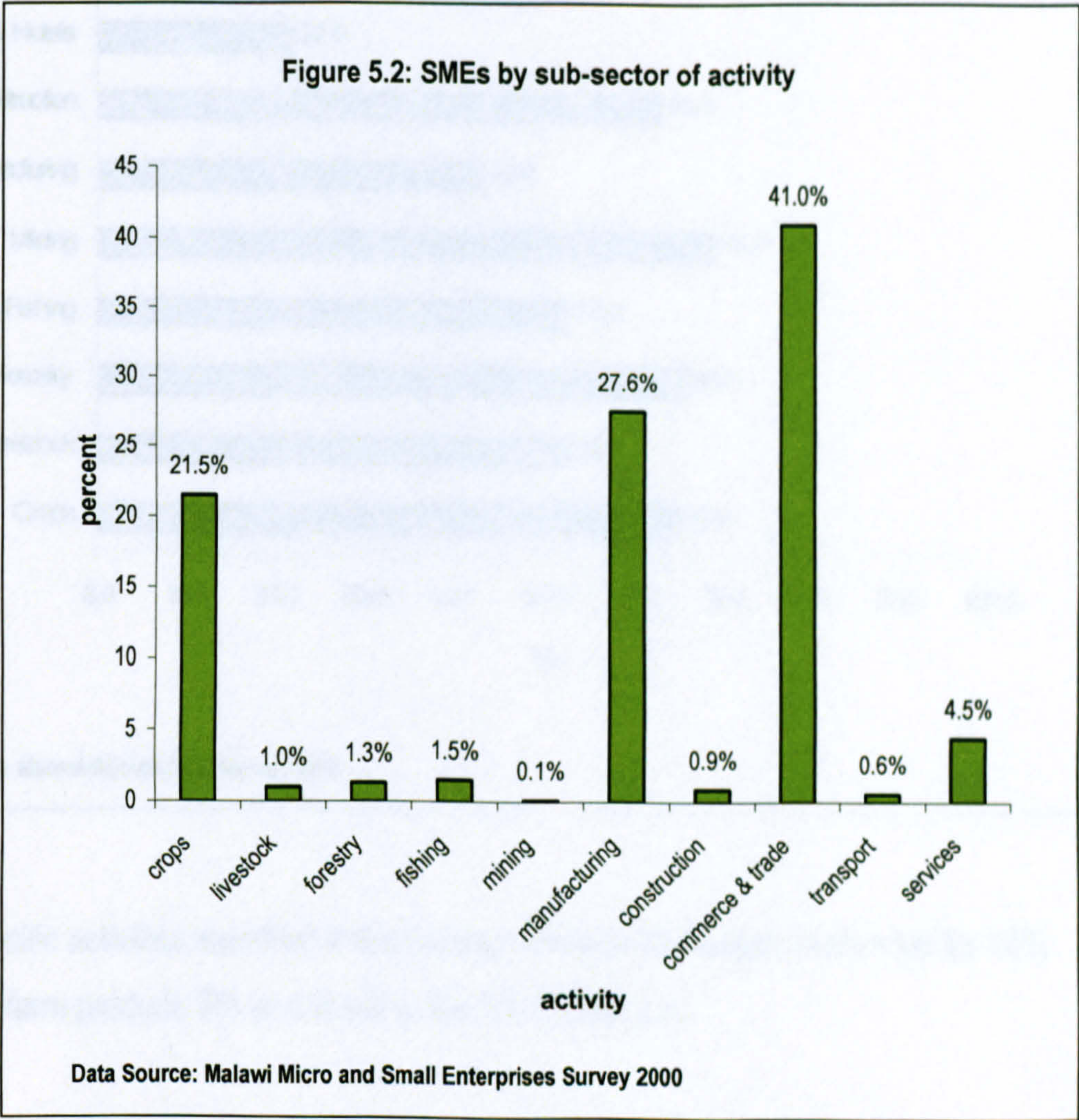
**Table 5.2: Characteristics of sampled enterprises by gender of owner**

Sub-sector of Activity	AGRICULTURE, MINING AND NATURAL RESOURCES						OFF-FARM EMPLOYMENT ACTIVITIES				
	Total %	Crops	Live-stock	Forestry	Fishing	Mining	Manuf-acturing	Constr-uction	Commerce Trade and Hotels	Transport	Services
<b>Gender of owner</b>											
Male	35.0	12.0	1.0	2.0	3.0	0.0	27.0	2.0	44.0	1.0	8.0
Female	34.0	4.0	1.0	2.0	0.0	0.0	43.0	0.0	46.0	0.0	4.0
Husband & wife	30.0	53.0	1.0	0.0	1.0	0.0	13.0	0.0	28.0	0.0	3.0
Other partnership	1.0	54.0	0.0	0.0	0.0	0.1	5.0	0.0	37.0	0.0	4.0
<b>% of employment</b>											
	100.0	36.2	1.3	0.6	2.7	0.1	20.8	1.1	32.7	0.8	3.7

Data Source: Malawi GEMINI MSE Survey 2000

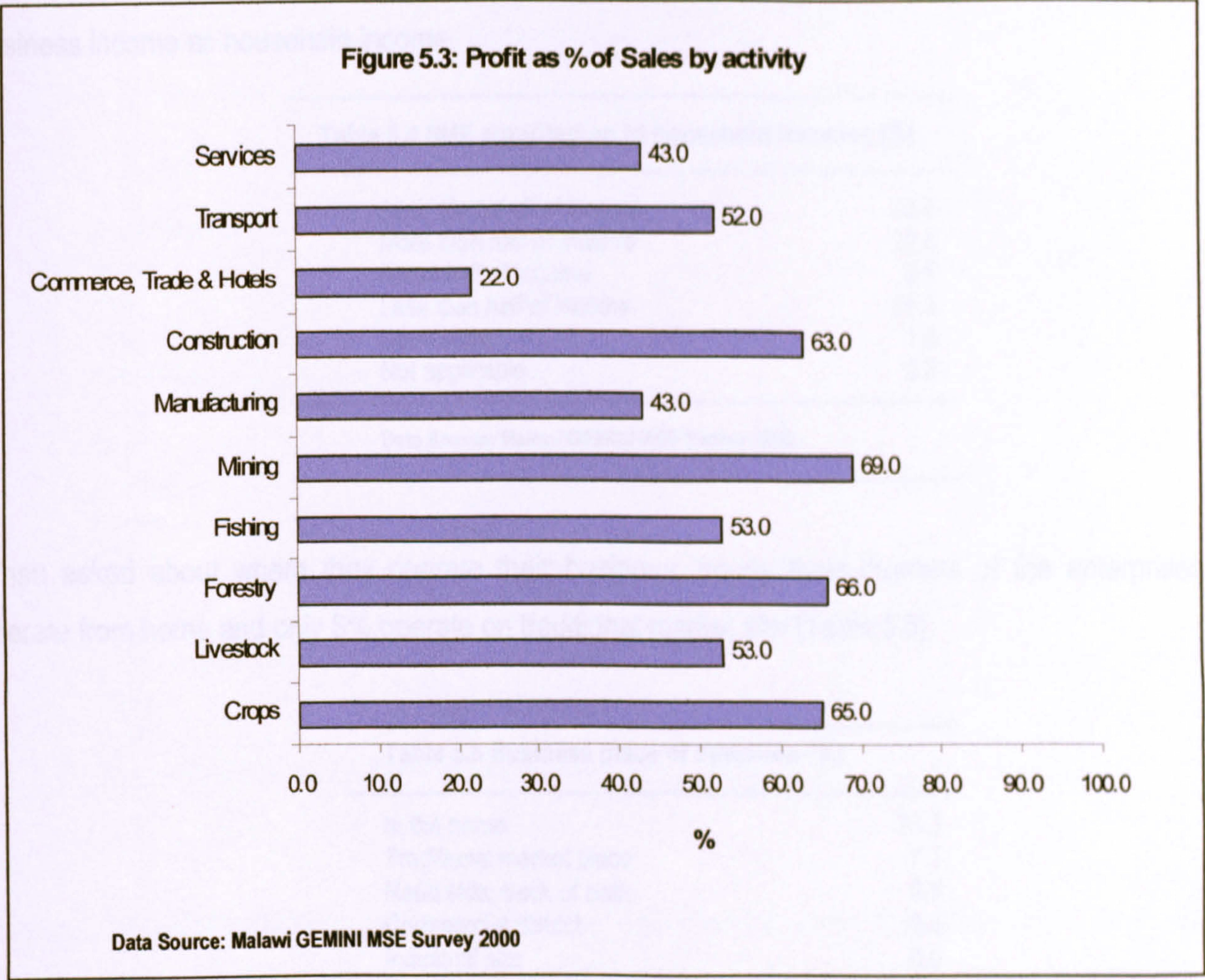


The sub-sectors of activities selected were: crops, livestock, forestry, fishing, mining, manufacturing, construction, commerce, trade and hotels, transport and services. And the leading sub-sectors were commerce and trade (41%), manufacturing (27.6%) and crops took a third place with 21.5% (Fig. 5.2).



Crop production offers more employment (36%) than any other sub-sector though it only accounts for 22% of the enterprises, whereas commerce, trade and hotels, where most enterprises are concentrated, offers 33% of employment, and manufacturing offers 21% of employment. As for profitability, the highest sales/profit ratio is in mining (69%) followed by forestry (66%), crops 65% and construction 63% (Figure 5.3). This is not surprising as these activities largely depend upon naturally occurring resources that the owners do not have to pay for, including the lake for fishing and land for farm produce.





When looking at specific activities identified in the survey, tobacco production accounted for 16% followed by vending farm produce 9% and vending fish 5% (Table 5.3).

Table 5.3 Dominant SME activities (%)	
Tobacco production	15.7
Vending farm produce	8.8
Vending fish	4.5
Local distilling	4.3
Bread, biscuit and cake baking	4.2
Beer brewing	4.1
Hawking	2.9
Grocery	2.8
Vending foods/sweets	2.5
Carpentry	2.1

Data Source: Malawi GEMINI MSE Survey 2000

Table 5.4 provides insight into the role of SME in the household and overall income contribution to the majority of people in Malawi. The survey revealed that just over a third of them use all of



income from their businesses towards household needs, and nearly 39.2% of all use half of their business income as household income.

Table 5.4 SME contribution to household incomes (%)	
All or almost all of income	33.6
More than half of income	29.6
About half of income	9.6
Less than half of income	25.2
Don't know	1.8
Not applicable	0.3
Data Source: Malawi GEMINI MSE Survey 2000	

When asked about where they operate their business, nearly three-quarters of the enterprises operate from home and only 8% operate on traditional market site (Table 5.5).

Table 5.5 Business place of operation (%)	
In the home	73.3
Traditional market place	7.7
Road side, track or path	9.7
Commercial district	2.4
Industrial site	0.0
Mobile business	3.4
Mobile market	2.9
Other	0.6
Data Source: Malawi GEMINI MSE Survey 2000	

The survey also revealed that over 70% of the SMEs had closed within five years of operation. Out of the female-owned SMEs, 78% close within five years of operation whereas 68% of male-owned businesses close within five years. Most of those SMEs in mining, commerce, trade and hotels and in forestry activities will close within five years of operation. Fishing businesses last longest with 50% of them having operated for more than 15 years. Overall, the SMEs in agriculture and natural resources last longer than those in manufacturing, commerce and transport services (Table 5.6).

The main reasons given for business closure included: finance problems (36%) with lack of operating funds being the main constraint; miscellaneous problems (28%); and 12.73% was accounted for by market problems, including lack of demand and too many competitors (Table 5.7).



**Table 5.6: Lifespan of businesses by gender and sector (%)**

	0 - 5 years	6 - 10 years	11 - 15 years	over 15 years	Total
	73	13	6	8	100
<b>Gender of owner:</b>					
Female	78	11	5	6	100
Male	68	16	7	10	100
Husband & Wife	72	14	7	8	100
Partnerships	87	13	0	0	100
<b>Sector of activity:</b>					
Crops	45	33	7	15	100
Livestock	42	47	0	10	100
Forestry	77	3	2	18	100
Fishing	34	16	0	50	100
Mining	100	0	0	0	100
Manufacturing	64	14	7	15	100
Commerce, Trade & Hotels	79	11	5	4	100
Transport	49	3	48	0	100
Services	57	11	23	9	100

**Source: Malawi Micro and Small Enterprise Survey, 2000**

Although the GEMINI survey distinguish between financial and market problems as reasons for business failure, these are related problems in some ways. On one hand there is lack of working capital (operating funds) and on the other hand there is lack of demand as the underlying causes for the failures. If there is too much competition from other SMEs, sales may go down due to reduced market share, and a fall in sales means less money for business operations.

Working capital problems could also be the result of poor cash management by SME owners. For example, owners could be diverting working capital to other personal usage rather than for running essential business operations, and also some cash is tied up with customers who take their time to pay back hence constraining business operations. These problems are to do with owners lacking proper training in management of the accounts receivable, which are paramount to survival and success of a business. To add another dimension, demand could be contracting due to poor performance of the economy as a whole and this would affect cash flows of the SMEs and lead to closure for some. An assumption is being made here that those business who indicated financial problems did not see market problems such as lack of demand as the main reason for their business failure. Without further information it is difficult to tell whether those who closed their businesses due to low demand had finances anyway to start another type of business or those who had inadequate operating capital just finished up and looked for someone to employ them.



<b>Table 5.7 Main reasons for business closure (%)</b>		
Financial problems	<b>35.69</b>	
Of which:		
Lack of operating funds		<b>75.0</b>
Lack of investment		<b>10.0</b>
Miscellaneous problems	<b>27.93</b>	
Of which:		
Household responsibilities		<b>32.0</b>
Poor health		<b>26.0</b>
Market problems	<b>12.73</b>	
Of which:		
Not enough demand		<b>38.0</b>
Too many competitors		<b>26.0</b>
Input problems	<b>12.20</b>	
Of which:		
Expensive inputs		<b>63.0</b>
Unavailability of inputs		<b>26.0</b>
Other reasons	<b>5.80</b>	
Started another business		<b>61.0</b>
Other positive reasons		<b>28.0</b>
Transport problems	<b>2.81</b>	
Labour problems	<b>0.78</b>	
Technical problems	<b>0.59</b>	
Government/regulatory	<b>0.49</b>	
Tools/machinery	<b>0.44</b>	
Shop/rental space	<b>0.42</b>	
Utility problems	<b>0.12</b>	
<b>Data Source: Malawi GEMINI MSE Survey 2000</b>		

When asked about business operation constraints, for the sample as a whole, three top most constraints mentioned were inputs problems (31.28%), marketing problems (30.12%), and finance problems (29.56%), Table 5.8. These main problems cited by the respondents give a good indication of the limits of their growth potential, which is restricted by the conjunction of three constraints: input constraints (expensive inputs); market constraints (not enough demand and very stiff competition); and finance constraints (lack of operating funds). Technical problems and problems with government and regulations were not cited frequently by enterprises as being constraints or reasons for closure.



Table 5.8 Business operation constraints (%)	
Inputs problems	31.28
Market problems	30.12
Financial problems	29.56
None	8.72
Miscellaneous problems	8.28
Transport problems	6.60
Tools/machinery	2.26
Labour problems	1.00
Government/regulatory	0.88
Shop/rental space	0.64
Technical problems	0.36
Utility problems	0.24
Other	0.10
Data Source: Malawi GEMINI MSE Survey 2000	
Note: Multiple answers were given by the respondents	

Of all sampled enterprises, only 15% received financial assistance (formal and informal credit), 23% received training and only 6% received business support such as help with business planning, management, marketing, design or technology (Table 5.9).

Table 5.9 SMEs receiving any form of assistance (%)		
Financial	15.0	
Credit institution		35.0
Agriculture input credit		34.0
Loan from friend/family		26.0
Banks		5.0
Training	23.0	
Free training from family		54.0
Training programme		16.0
Paid apprentice		16.0
Vocational/technical		12.0
Self-trained		1.0
Other		1.0
Business support	6.0	
Business management		32.0
Technology/production		40.0
Business planning		17.0
Design		6.0
Marketing		5.0
Data Source: Malawi GEMINI MSE Survey 2000		

Of those who received financial support, 35% received funds from credit institutions, 34% received agricultural inputs and 26% got loan from family or friends. For those who received training, most of them (54%) got it for free from family, and this is usually provided on the job when younger and



obviously plays a significant role to SMEs. With some of the training being provided by family members, it raises concerns over the value of support and consequently quality and relevance of the training itself.

When contrasting 2000 GEMINI survey results with 1992 results, it was revealed that there have been some shifts in the SME sector. There has been an increase in number of urban SMEs (from 11% to 22%), more than matching the marginal increase of urbanisation in the country. Overall, there appears to have been a 5% decrease in the off-farm SME activities (manufacturing, commerce and trade and services) and the decrease was confined to rural areas. However, since the primary production based enterprises (agricultural and natural resources) were not covered in the 1992 GEMINI survey, it is difficult to tell whether at that time there had been a shift from the secondary to primary production based SMEs. Since 1992 there was been a slight increase in the proportion of SMEs engaged in trade (52% in 1992 and 54.9% in 2000). In terms of enterprise dynamics, 80% of the firms were stagnant and served primarily as additional sources of income for households whereas only 20% of them were growing and re-investing some or all of their profits into the firms. The 2000 survey revealed that natural resource based sectors (fishing, mining and dairy) was growing at faster rates usually yielding more profits to the owners. The survey also found that current support services had focused on institutional support especially for credit institutions. There has been some training and other limited business support services – but all these efforts were reaching very few people, no more than a quarter of the people involved in SME activities.

Although the Integrated Trade and Industry Policy of 1996 was formulated, it should be noted that there have never been policies and strategies specifically designed for the development of the SME sector in Malawi until recently. The SMEs have had to operate within policy framework of large-scale enterprises, for many years, which did not take into account of SME-specific constraints. Moreover as most SMEs operate outside the formal sector, it not surprising that the institutional support and strategies does not reach out to most of them. In order for the government support to be helpful and reach out to those who need it most, policies which are specific for the informal SME sector would be needed, as well as monitoring in order to ensure that the most needy and vulnerable are also being reached and helped. There are enough of institutions in Malawi (MEPC, DEMAT, SEDOM to name a few) which have been established to support the SME sector in the form of training provision, business advisory services, market information and credit finance. Indeed, despite an increase in magnitude of these support institutes, so far indications are that the support which these institutions is not reaching the intended targets, not to mention if the type of



support itself is appropriate for SMEs, particularly the informal ones. Appropriate government policy which encourages the development of strategies for things like cash management would be more helpful than just setting up credit institutions.

Without a doubt, Malawi's SME have been affected by the policy reform changes discussed in Chapter Four, and these policies could have affected SMEs in a number of ways. With the policy of trade liberalisation, imports of all kinds including consumer goods have been allowed into the country. While an increased degree of "openness" may also create opportunities for increased manufacturing production for export purposes, it may generally be the case that only firms larger than 50 workers are in a position to take advantage of those opportunities. The increased proportion of SMEs engaged in trade (mainly small-scale vending) may also be an indirect result of the structural adjustment process. Decreased real incomes may cause an increase in demand for the consumer products sold by SMEs. However, several studies in Malawi have shown that increasing tobacco incomes have led to increased effective demand for traded goods and that rural trading activities have grown at a much higher rate around tobacco producing areas (Daniels and Ngwira 1993, Makawa 2000, Simons 1999).

## **5.4 Summary**

The main objective of Malawi's 2000 GEMINI style-based survey of micro and small enterprises was to provide a relatively complete and detailed understanding of the current status of the sector, including distribution of SMEs by sector and ownership, business characteristics and actual contribution to employment and incomes. The survey revealed the SMEs are significant and critical sources of income for both rural and urban households and providing income to most households in the country. Sectors showing strong market growth potential are natural resource-based (fishing, mining and tobacco). In a country like Malawi which has a very low per capita income, there is limited internal purchasing power so products for export will offer stronger possibilities for growth. In previous micro-enterprise studies, primary production in agriculture and natural resources sectors have traditionally been addressed in the context of providing raw materials for off-farm activities but not as enterprises in their own right. The 2000 study examined primary production as an enterprise itself, and this provided insights into Malawi's persistent attempts to effect the transition from subsistence production as a traditional way of life to agricultural production as a business and income generating activity especially among the rural populations.



## Chapter Six

### Survey Findings

#### 6.1 Introduction

The aim of this chapter is to analyse the degree to which expectations of structural adjustment policies have been realised in Malawi. An empirical investigation on the SME sector was conducted to analyse the effect of SAPs and globalisation on the sector. The survey and data collection methods have been covered in Chapter Three. Although this research is to a large extent empirical, the presentation and interpretation of the survey results, analyses of impact of globalisation and trade liberalisation on SME development and responses of the SME sector to the reforms can only be meaningful if they are seen in the context of globalisation and Structural Adjustment Programme measures.

The results of the survey have been interpreted in the light or darkness of globalisation and marginalisation. Within this context (brought together in Figure 1.1), the present empirical investigation looked at the impact of the SAP measures on the SME sector, analysing how the SMEs have coped with the changed environment and how competitive or not they are becoming in the face of external competition. Major factors that are currently significant determinants of SME global competitiveness, which were examined, included inter-firm relations, technology, finance, infrastructure, training, and support from government and external institutions. The impact of adjustment was measured by analysing the responses to questions regarding market share/access, productivity, competition, export growth, industrial growth and so on as these were the factors supposedly facilitating SSA country integration into the global economy. Therefore the ultimate purpose of the empirical research was to determine whether integration is happening, or whether Malawi is being further marginalised.

The following sections provide a description and analysis of the findings on the impact of globalisation and the Structural Adjustment Programme on the small enterprise sector in Malawi. It should be noted that, although analysis tables distinguish three categories of SMEs (1-4, 5-20, 21-50) as in the GEMINI surveys, the discussions centres around and refers to the '1-4' category as micro and the '5 and over' category as small since there was only a very small number of enterprises with over 20 employees in the sample. In the first sections, analysis of findings from the in-depth interviews with Government and NGO officers is presented, followed by an analysis of results from the entrepreneur survey.



## **6.2 Analysis of the Data**

The underlying phenomenon and mechanisms of the effects of globalisation and economic reform measures has been brought to light partly through literature review and partly through an empirical investigation. As the empirical investigation was carried out in two phases, data gathered has also been analysed and presented separately in the following sections.

### **6.2.1 Analysis of findings from Phase I investigation**

Findings from this phase of the survey are based on the knowledge and discussions drawn from the unstructured in-depth interviews held with highly positioned experts working in governmental and non-governmental organisations in Malawi, supplemented by background material and documents obtained from the interviewees. It is not possible to be definitive about the impact of trade policy reforms since some of the respondents indicated that substantial reforms had just taken place relatively recently. As noted in Chapter Four, trade policy reforms were launched in 1988, well after the start of adjustment reforms in 1981. In addition, structural policy reforms in the critical area of factor markets such as power, telecommunications and transport had just begun fairly recently, around 1996. Another important point to note from the results is absence of a significant difference of opinion, on the issues discussed, between the government and NGO participants interviewed in this study.

Since conversations were recorded in note form, the materials were transcribed by indexing responses and conversations with respect to theory underlying the research. Issues were categorised into the following concepts: Globalisation; SAP; Trade Liberalisation; Competition; and Strategy/Policy issues. The findings have been presented in Boxes 6.1 to 6.5. For detailed responses see Appendix 5.

#### **6.2.1.1 Globalisation**

One common indicator of globalisation is the extent of investment flows and this includes both physical and portfolio investments. In the case of Malawi, both portfolio investment and the flow of Foreign Direct Investment are insignificant. There are many reasons why private investment in general and FDI in particular have not increased significantly over the years. Reasons noted from respondents and document sources range from the poor infrastructure, crime and theft, inflation and corruption as major obstacles to private businesses. It has been noted in a World Bank report that foreign investors who might otherwise be attracted by Africa's cheap labour are deterred by the problems of doing business in countries where the rule of law is so weak that even simple contracts can be difficult to enforce, and where businesses that do persevere have to bribe many poorly paid



bureaucrats who can otherwise make business impossible (World Bank 2005b). The general consensus amongst respondents was that 'globalisation' is not happening for Malawi. The analysis on trade-related indicators of globalisation also suggested that there was no marked difference in terms of Malawi's degree of integration during the post-reform period compared to the pre-reformed period (UNDP/UNCTAD 1999).

Not many issues were raised around 'globalisation' itself; respondents were more interested in discussing the effects of trade liberalisation and competition from outside. These two items appeared to be the 'hot' topics of the time amongst the policy-makers in Malawi. However, for those who took an interest in 'globalisation', they felt that Malawi is not being integrated into the global economy and that there was no level-playing field yet. One interviewee even commented that "Malawi has not entered globalisation as such, what is being experienced now with the opening up of trade is internationalisation". He strongly felt that 'globalisation' is about investing in another country with that country enjoying the benefits of the investment as opposed to all profits being drained out of the country as is currently happening in Malawi (Box 6.1).

**Box 6.1: Respondents' perspectives on the Globalisation concept**

- We need to distinguish between globalisation and internationalisation
- Malawi has not experienced globalisation yet. What is being experienced now with opening-up of trade is internationalisation
- Companies are coming from outside to make money here and take the profits out without re-investing in the country. It feels like we are being exploited
- There is more exploitation going on as assets are not shared with the locals
- There is no tangible investment being made to make Malawi grow economically
- The level-playing field is not there
- Malawi is not ready for globalisation and most SMEs do not have the necessary knowledge and skills to recognise the opportunities and benefits of globalisation

There was a feeling amongst the respondents that some sort of exploitation by foreign investors is going on in the country. The concern expressed was that foreign investors come in the country and set up their businesses but then take out all the profits they have made to spend in their country of origin. Thus, foreign investment does not provide much benefit to Malawi in terms of transfer of knowledge and technology, wealth creation and economic growth. The interviewees' main concern was that foreign investment in Malawi, far from enriching the country, is later being returned to the industrialised world through repatriated profits, artificially low prices for developing-country exports, and high interest payments on the country's debt.



### 6.2.1.2 Structural Adjustment Programme

There was a general consensus amongst the interviewees that the Malawi economy has undergone de-industrialisation as a result of policy reforms under the adjustment programmes of the last two decades. They believed that trade policy reforms had been exceedingly rapid and dismantling of protection had led to the contraction of significant sections of the manufacturing sector in Malawi, which was not been given enough time to increase their competitiveness and hence lost out to competition from imports. Thus in the words of one interviewee, “there has been dis-investment in manufacturing and Malawi has been transformed from a producing to a trading economy because of liberal trade policy”. This is a very important point to note because a World Bank document indicated that Malawi’s long-term growth depended on the rapid growth of the manufacturing sector (World Bank 1997a). The issue of the decline of the manufacturing sector came up in almost all the discussions with the interviewees who gave the examples of the collapse or scaling down of operations of some of the country’s well-known companies such as David Whitehead & Sons, a textile manufacturer; Unilever; Mulanje food processors; and Shire bus company, whose failures were attributed to free trade policies.

Due to removal of price controls and the parastatal monopolies (ADMARC, MDC and PCL), discussed in Chapter Four, small traders are now active in all parts of the country in retailing of household and consumer goods. It appears the various reforms have closed some doors while opening others as one of the interviewees pointed out that, “manufacturing sector has lost out whereas distribution, retail and professional services are not doing too badly”. This could be seen as a compensation in some ways but still not enough to boost the economy as trading and export of own country’s manufactured goods is required for economic growth. It has been shown that Malawi experienced lower average rate of growth of real GDP during the SAP period (1981-1998) than during the pre-SAP period (1971-80) (Malawi Government 2001). Amongst reasons given for the slow growth rate were exogenous shocks, decline in rate of gross domestic investment and a decline in the rate of growth of exports. However, these were not the only reasons attributed to this situation, drought and suspension of non-humanitarian aid in 1992 also slowed down the economic growth as was pointed out by some respondents (Box 6.2).

The main point noted from the discussions was the fear and disappointment expressed amongst both governments and NGOs officials that economic growth has slowed down and that it will continue to do so if manufacturing and industrialisation are not encouraged. They feel that the economy will become worse if people continue to consume goods from outside the country and not



engage in production themselves. Almost all of the respondents would like to see the industrialisation process led by SMEs since a lot of these have mushroomed due to liberalisation of trade.

**Box 6.2: Respondents' perspectives on the SAP concept**

- There has been no positive impact as far as opening up trade is concerned
- Since the number of SMEs continues to grow, they should be encouraged to lead the industrialisation process
- There has been slow-down of economic growth since the SAPs
- Initiatives being implemented are not coordinated
- There have been problems with management of the economy
- The manufacturing sector is losing out whereas it seems distribution, retail and professional services have benefited
- The SAPs attached conditions which prevent the government from helping out or coming up with its own strategy to develop the manufacturing and production sector
- SAPs did not make a provision for how to cope with competition as many of our SMEs don't have the technology or technological know-how necessary for being competitive
- Drought and suspension of aid in 1992 did not help matters in terms of economic growth
- There has been dis-investment in manufacturing and Malawi has been transformed from a producing to a trading economy because of liberal trade policy.

However, it was also noted from respondents that while neo-liberal policies are desirable, they are not sufficient to place Malawi in the right position for global competitiveness since the country itself is not ready and equipped to compete due to the reasons mentioned above. What was immediately apparent was the acknowledgement of the importance of technical and technological modernisation as a factor in determining the way in which small firms respond to structural adjustment.

### **6.2.1.3 Trade Liberalisation**

Most of the interviewees thought that Malawi had become a 'trading' nation where production and manufacturing were decreasing. This was meant in the sense that most entrepreneurs were just involved in purchasing finished goods from abroad and selling them to local consumers without the country having equivalent amount of exports of its own for economic growth. This has become a big problem for the country in terms of loss of foreign exchange leading to deficit in balance of payments. The concentration of 'trading' activities could be seen as a problem as it is an aspect of de-industrialisation. This is evidenced by the increase in numbers of large-scale producing enterprises (with greater export potentials) which are folding due to competitive imports by individuals. Manufacturing sectors with potential growth are the ones that are decreasing production and most of them are closing down. Food processing, bakery, textile and weaving were the frequently mentioned sectors with great potential for growth, but due to competition from imports, nearly all have been eroded.



### Box 6.3: Respondents' perspectives on Trade Liberalisation

- Malawi has become a 'trading' economy with not much of production happening
- Manufacturing cannot prosper with the poor infrastructure
- There is limited access to foreign markets and people need to be trained on how to access these markets but there is no money for this
- There are only a few export commodities, mainly agricultural
- There are a few exports to South Africa, and there is an ongoing dispute over export volumes to Zimbabwe. Potential export products include textiles, small-scale mining and tourism
- The country opened up too much hence attracted a large influx of imports and cheaper goods
- Trade liberalisation was imposed by IMF and World Bank and we were not pre-warned of the downside of it when it was being encouraged
- There is no law for small-scale taxing hence informal trade has resulted in government's loss of revenue
- Trade liberalisation is encouraging laziness
- As regards to 'free trade', manufacturing sector has lost out whereas distribution, retail and professional services have gained
- The country rushed with liberalisation
- There have been drops in manufacturing of textiles and food processing
- Volume of other products has grown whereas others have retreated
- Tobacco prices are being depressed
- Some local businesses feel that incoming investors have been given preferential treatment
- Production is decreasing and yet production creates employment
- There is no policy or strategy to manage the trade liberalisation process
- SMEs have small production units which cannot meet demand
- Most imports are luxuries
- There is no control on foreign exchange hence country is losing out money
- There is no emphasis on entrepreneurship
- We should not have liberalised everything, there is a need for control on some key products
- Not much consultation with local producers as regards to international trade agreements
- There have been drops in manufacturing of textiles and food processing due to lack of the necessary technology to produce competitive products.

Most of the respondents attributed the collapse of the manufacturing sector to poor infrastructure and lack of necessary technology to produce competitive products. The following were some of the comments made by the respondents regarding foreign markets and production machinery: "...Malawi has been given a quota to export textiles to the US but we are failing to do so because the textile we produce is of poor quality and the production process is very slow due to obsolete machinery and frequent electricity power cuts"; "there is limited access to foreign markets and people need to be trained on how to access these markets but there is no money for this"; "there are only a few export commodities which are mainly agricultural ...potential export products include textiles, small-scale mining and tourism, the potential which we are not maximising due to out-of-date machinery".

Liberalisation of foreign trade and the foreign exchange market has provided business opportunities to SMEs engaged in pure buying and selling, but the positive impact on those engaged in actual



production does not appear to be clear. Some old and new SMEs are now engaged in import trading of goods mainly sourced from neighbouring countries (particularly from South Africa and Zimbabwe) whose industries have a competitive edge over Malawi. Others are engaged in selling second-hand clothing sourced from developed countries. The second-hand goods are sold at very low prices relative to new goods, which have provided some relief especially to poor households in rural and urban areas. However, there needs to be a balance between Malawi's longer-term growth aspirations and the immediate consumption needs of the poorer social groups. It could be argued that whilst consumers are benefiting from buying very cheap imports, manufacturing SMEs cannot flourish if their potential markets are saturated. The flooding of imported consumer goods into Malawi, which are generally cheaper than similar goods produced locally by some SME (and large firms), has adversely affected SME output and employment. Little is exported by the Malawi SMEs and interviewees attributed this to lack of knowledge of export markets and how to access them.

At the regional level, Malawi is facilitating its trade through the COMESA and through the SADC. The trade liberalisation measures of the COMESA include a gradual reduction of all tariffs imposed on a range of selected commodities over a ten-year period and later tariff cuts to extend to all goods. SADC encourages bilateral trade deals between member states in order to facilitate intra-regional trade although some respondents were not happy with the way these trade deals are arrived at and conducted. Respondents felt that the provision and use of non-tariff barriers by Zimbabwe, in the form of export restraint and bureaucratic rules that are designed to make it difficult for the Malawi goods to enter the country has led to an increase in trade imbalance in favour of Zimbabwe. There seems to be no provision for dispute settlements, and it appears that these agreements were not carefully negotiated. "...and there is an ongoing dispute over export volumes to Zimbabwe...", to quote one of the respondents. Moreover, trade continues to be constrained by other non-tariff barriers such as communication problems, border procedures, lack of information, import licenses, surcharges (form of tax), transport problems and foreign exchange problems (Malawi Government 1998). Trade disputes settlement is one of the new functions of the World Trade Organisation's approach towards free market. The WTO provides a forum for multilateral trade negotiations and to settle trade disputes related to General Agreement on Tariffs and Trade (GATT). It could be the case that Malawi has no confidence in the WTO or lacks the resources and expertise to carry out trade the negotiations or to bring the trade disputes to the WTO forum for settlement.



#### **6.2.1.4 Competition**

From the discussions with participants, it appears that domestic demand is being satisfied through imports of goods and services, an environment, which is not conducive to economic growth. This is supported by a report by the National Statistical Office, which described a substantial decline in the productivity of most sub-sectors including food processing, textiles and weaving 1994 due to stiff competition from imports (Malawi Government, 2000b). The government officials interviewed were concerned that if domestic demand was being satisfied through imports, this could lead to serious balance of payments deficit because the country is living beyond its income/means. According to one interviewee, "Malawi's low manufacturing capability has raised the domestic market share for the imported manufactured goods up to 95% this year". If that is the case then this may either lead to more borrowing and debts or there will be an increase in money supply, which will undermine price stability. On the other hand, consumers appear to be the sole beneficiaries from the competition since the informal sector has grown so rapidly that it is eroding the market for locally manufactured goods as it provides goods at affordable prices, though this may be creating conflict between consumption and growth. It should be noted that this assumption may not be true as consumers were not interviewed to ascertain whether the imports were more affordable than the local goods. This could be a potential area for further research.

The main reasons given by the respondents for uncompetitive local products were high transport costs, obsolete technology, poor infrastructure in terms of poor road conditions, and lack of necessary knowledge and skills to recognise the opportunities and benefits of globalisation and free trade. The rigorous application of liberal measures has brought existing manufacturing enterprises into severe difficulties and large ones have lost their monopolistic character in the face of competing imports. While there is a favourable effect through reduced pricing of goods through cheap imports, trade liberalisation has precipitated the collapse of producing enterprises, fundamental to export growth. One of the major concerns expressed by the respondents was that Malawi's production sector is facing serious supply constraints and that as a result, her exports are not competitive. This is principally due to high costs of imported inputs caused by currency devaluation, payment of import duties and surtax on most of these inputs. Other factors, mentioned, contributing to the high cost of production were an unsatisfactory state of the internal road networks, frequent cuts in power and water supply, inefficient telecommunications services and a high rate of crime which necessitates large expenditure on security.



In 2001 it was reported that, poor communication infrastructure and micro-finance facilities resulted in only 10% of agricultural produce to reach the market, resulting in extra reduction of the market share for domestic goods (Malawi Government 2002), which is unfortunate as this was a missed opportunity for local producers. High costs in the use of road transport and poor trading arrangements (lack of synergies among the local producers) inflated prices of local goods thereby making domestic goods uncompetitive in the domestic market. Lack of a competitive environment was frequently cited as one of the reasons why the manufacturing sector was falling and why the industrial sector is dominated by very few firms (Box 6.4). Absence of competition policy was leading some sub-sectors to engage in restrictive business and unfair trading practices. Some of the sub-sectors, mentioned in the competition policy document, that were engaged in restrictive business practices included transport, health, private clinics and legal services. For example these service industries, through associations, would agree on minimum charges and even make arrangements of market sharing which is a predatory and exclusionary behaviour not to mention detrimental to consumer welfare (Malawi Government 1998). However at the time of interviews the government had just drafted the competition policy document, which put in place clear policies and legislation to foster a proper competitive environment for business enterprises.

#### **Box 6.4: Respondents' perspectives on Competition**

- Large-scale enterprises are collapsing and shutting down due to competitive imports
- Industries are not well-equipped for competition. Transport cost is too high for them and most of them use obsolete technology
- There are a lot of infrastructural problems such as electricity, water and roads are very poor and this impacts on productivity
- No capacity, infrastructure and necessary technology to produce competitive products
- SME constraints need to be addressed and focus on areas of high growth
- High inflation and interest rates have affected businesses
- Human resources not trained and unproductive cheap labour hence we cannot compete
- Less value is attached to local products and value-adding to products is very minimal
- There are no inter-industry linkages between enterprises
- Malawi cannot compete on the international scene
- There are no safeguards for the domestic market
- Competition is very strong. Cheaper and good quality imports are competing with local products
- Only efficient enterprises will survive
- Malawi's low manufacturing capability has raised the domestic market share for the imported manufactured goods up to 95% this year
- No studies have been carried out on how competitive Malawi enterprises have become due to free trade
- Competition policy has just been drafted
- Local products are uncompetitive due to high transport costs, obsolete technology and poor infrastructure. For instance, the internal road network is well below basic standards
- Competition is very stiff these days and not many firms are surviving within this environment. It is especially tough for manufacturers
- Crime has gone up considerably and this has become a problem for businesses because they end up spending a lot on security



As discussed in Chapter Four, the bulk of manufacturing activities are highly dependent on agriculture and natural resources as sources of raw materials. Assuming that Malawi's comparative advantage lies in agriculture and natural resources, the agro-based industries are supposed to generate the highest social gains from the use of land and labour resources if used in the most efficient way. But the Domestic Resource Cost analysis (one of the most commonly used tools for measuring comparative economic advantage of a country) carried out by the Malawi government, suggested that, in general, agro-industries in Malawi exhibited a lack of long-run competitiveness (Malawi Government 2002). However, some of the sub-sectors that exhibit competitiveness in the short term include food processing, beverages, apparel and textiles. Respondents pointed out that there was a need for more investment in new technology for these sub-sectors to be more competitive. At present, SMEs face an acute problem of limited access to appropriate technologies to enable them to produce goods of high quality for the export market. In the view of respondents and supported by strategy documents, major constraints faced by the manufacturing sector of SMEs, include limited linkages with large-scale enterprises, use of mature technology, inadequate standards and quality assurance and limited international marketing capabilities. They said production capacity had fallen to low levels mainly due to lack of spare parts, poor maintenance and frequent downtime of machinery.

#### 6.2.1.5 Strategy and Policy issues

When the respondents were asked to comment on strategies for developing the SME sector, they pointed out that the main focus for the development of the manufacturing sector would be to widen and strengthen its base with a view to lessening dependence on a few sub-sectors (Box 6.5). Hence the primary strategy would be to identify new sources of growth to accelerate the expansion of the manufacturing sector.

##### Box 6.5: Respondents' comments on SME strategy and policy

- Although the new Poverty Reduction Strategy recognises SMEs critical stakeholders, it has come too late as half the population is below poverty line
- Marketing of the country and products need to be done vigorously so that people can be encouraged to engage in production
- Some form of intervention by the government is required in some selected sectors such as the textile industry

The respondents felt that there was a need to achieve greater added-value and linkages both vertical and horizontal, especially in resource-based industries. They pointed out that emphasis



should be placed upon development of competitive industrial clusters through integration of key industries, suppliers, supporting industries and critical supporting businesses services and that there is a need to develop value chains with significant backward and forward linkages with more emphasis on SMEs. The Malawi Poverty Reduction Strategy Paper (MPRSP) identified the following industry cluster groups for development, promotion and support: textiles and apparel; agro-based and food products (cassava, pulses, fish, livestock, fruits and vegetables); resource-based industries (wood, gemstones, handicrafts); chemical products (pharmaceuticals, fine chemicals); engineering industries (automobile consumables and components) and consumer manufacturers.

It has also been suggested by some analysts in Malawi that the supply constraints may be overcome by establishing small producer cooperatives and production centres with common facilities which would enable SMEs to pool resources and wield more bargaining power (Thindwa 1996). This would enable them to meet large export orders directly or through subcontracting with large firms, which at present is not practiced in Malawi. Respondents also pointed out that Malawi needed a transition period during which it could have identified production and market niches that favour its competitive advantages in the context of the emerging world division of labour and once this was achieved it could then fine-tune its commercial practices. There was no provision in the SAPs to help with the transition process from closed to open market economy as this was left for individual countries to deal with, and it is still proving to be a problem to this date in the case of Malawi. A properly planned transition period (incorporated within the SAPs before implementation) might have helped and made a big difference for the country's integration process through well-articulated trade policies and bilateral and multilateral assistance to augment its capacity to integrate into the world economy.

### **6.2.2 Analysis of findings from Phase II investigation**

This section presents the analysis of the findings of impact of the reform measures from the small and micro-scale entrepreneurs' point of view. For this particular analysis, impact of the structural adjustment programme on characteristics of SMEs was analysed under three main headings: the Entrepreneur, the Enterprise and the Business Operating Environment. These segments are not, however, rigid since areas under these headings overlap to a large extent. Two criteria were taken into account for the processing and analysis of the results: size of enterprise and sector of activity. Two enterprise sizes were defined according to number of permanent staff (as per definitions in section 5.2), amalgamating the 5-20 and 20-50 employee-size categories.



Nine sub-sectors of activity were created from the survey results and these were: food products; building and construction; construction materials; wood products/furniture; metal products; clothing/tailoring; woven products; services and groceries/hawkers. The services category included plumbing, electric repairs, hair-dressing, telephone bureaux, minibus service, private clinics and private schools. Enterprises that did not fit into any of these sub-sectors were classified as 'miscellaneous industries'.

As noted, there were a total of 147 participants surveyed in this phase of the study. Out of the 147 firms surveyed, 63% were micro-enterprises, 37% were small enterprises with only 4% out of them having more than 20 employees. The breakdown of the sample by sector of activity was as follows: food products (27% of the enterprises); services 25%; wood products/furniture 10%; clothing/tailoring 10%; building and construction 5%; metal products 4%; construction materials 3%; woven products 3%; groceries/hawkers 3% and miscellaneous industries 10% (Figure 6.1).

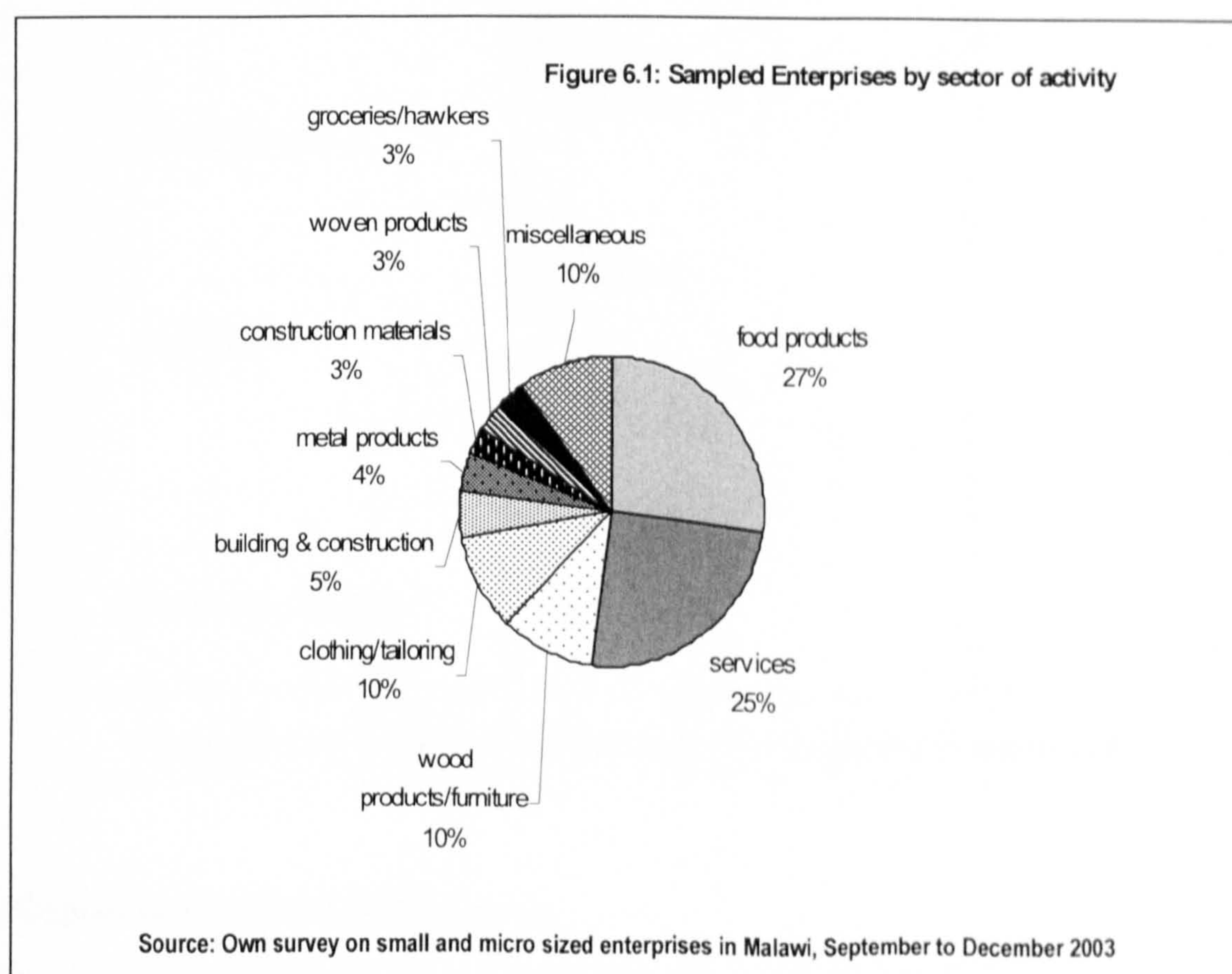


Table 6.1 shows the characteristics of the sample by size of enterprise, sector of activity and year of creation, thus, distinguishing those enterprises created before from those created after 1981, when the first SAP measures were introduced. Only 11% of the surveyed enterprises were created between 1981 and 1988, a period corresponding with the introduction of the first measures of the



SAPs. As Table 6.1 shows, more than 50% of the enterprises were created after 1994, a period corresponding with political liberalisation rather than trade liberalisation. Nearly 70% of the enterprises established after 1994 were in three sub-sectors of activity: food products (31%), services (24%) and clothing/tailoring (14%).

Table 6.1: Characteristics of sample entrepreneurs and enterprises			
		No.	%
Size:	Total	147	100.0
	Micro (1-4)	93	63.3
	Small: (5-20)	48	32.6
Created:	(21-50)	6	4.1
	Before 1981	6	4.0
	Between 1981 and 1988	16	10.9
	Between 1988 and 1994	47	32.0
	After 1994	78	53.1
Belonging to:	Male	85	57.8
	Female	44	29.9
	Husband & Wife	15	10.2
	Other Partnerships	3	2.1
Educational Level:	None	4	2.7
	Primary	44	29.9
	Secondary	65	44.2
	Technical/College	22	15.0
	University	12	8.2
Age Group:	16-20	1	0.7
	21-25	11	7.5
	26-30	17	11.6
	31-40	75	51.0
	41-50	29	19.7
	Over 50	12	8.2
	Missing values	2	1.3
Formal business training:	Yes	36	24.5
	No	111	75.5
Source: Own survey on Small and Micro-sized enterprises in Malawi, September to December 2003			

### 6.2.2.1 Characteristics of the Entrepreneurs

Estimates on the age distribution of owners of SMEs showed that over 75% of respondents in the sample were younger than 40 years of age (Table 6.1). The average age of entrepreneurs was 36.6 years (range 20 – 65 years). These are not surprising results as they reflect on the Malawi's population age distribution: half the population is under 15 years of age, and only 4% are over 65 with life expectancy of 40 years in 2005 (section 4.2.3). The distribution of educational standards indicated that 97% of the entrepreneurs had gone to a formal school. These are surprising results



considering that the country's literacy rate was only 62% in 2000 (Government of Malawi 2000). Nearly 70% of SME owners had attained secondary and college/university educational level. The higher educational standard of entrepreneurs stands the SMEs in good stead, since as has been suggested elsewhere, that entrepreneurs with higher educational training standards are more likely to survive economically in a more 'turbulent' business environment (Anheier and Seibel 1987). The entrepreneurs who received most schooling (technical/college and university) were found in the services sub-sector, whereas those with education of up to primary school level were mostly into selling groceries and construction materials. These findings suggest that due to high unemployment rate, young and educated people who would otherwise have sought jobs in the civil service and other public organisations now set up small-scale businesses, and that most of the entrepreneurial activity is out of necessity or adversity.

Although a majority of the sampled entrepreneurs had attained at least secondary school education, business training was very limited, as the results on training indicated that few people had any formal business training at all. Only 25% of the entrepreneurs had had formal training in business skills and most of it was in how to run a business and in the areas of sales and marketing. Some, however, received training in areas that would be considered somewhat obscure by many, such as how to make hoes, chicken feed or chairs. This is a serious limitation which results in lack of proper management, especially in such matters as financial records and bookkeeping. The picture that emerges is of a young and educated small-scale entrepreneur, who lacks vocational/technical training. Training in matters such as market analysis, good record-keeping, management of cash receivable are paramount to SME performance. Therefore even if most proprietors may have received formal mainstream education, without emphasis on any of the mentioned relevant business training, chances of survival of the business would be very slim, no matter how much financial assistance (which is mostly made available to medium-sized enterprises anyway) may be made available to them. Training on how to manage working capital and keeping records of all business transactions and operations is very significant. And as said before, this is probably the area where the government may need to focus on, ensuring that it is targeted to and reaching micro and small-scale enterprise entrepreneurs.

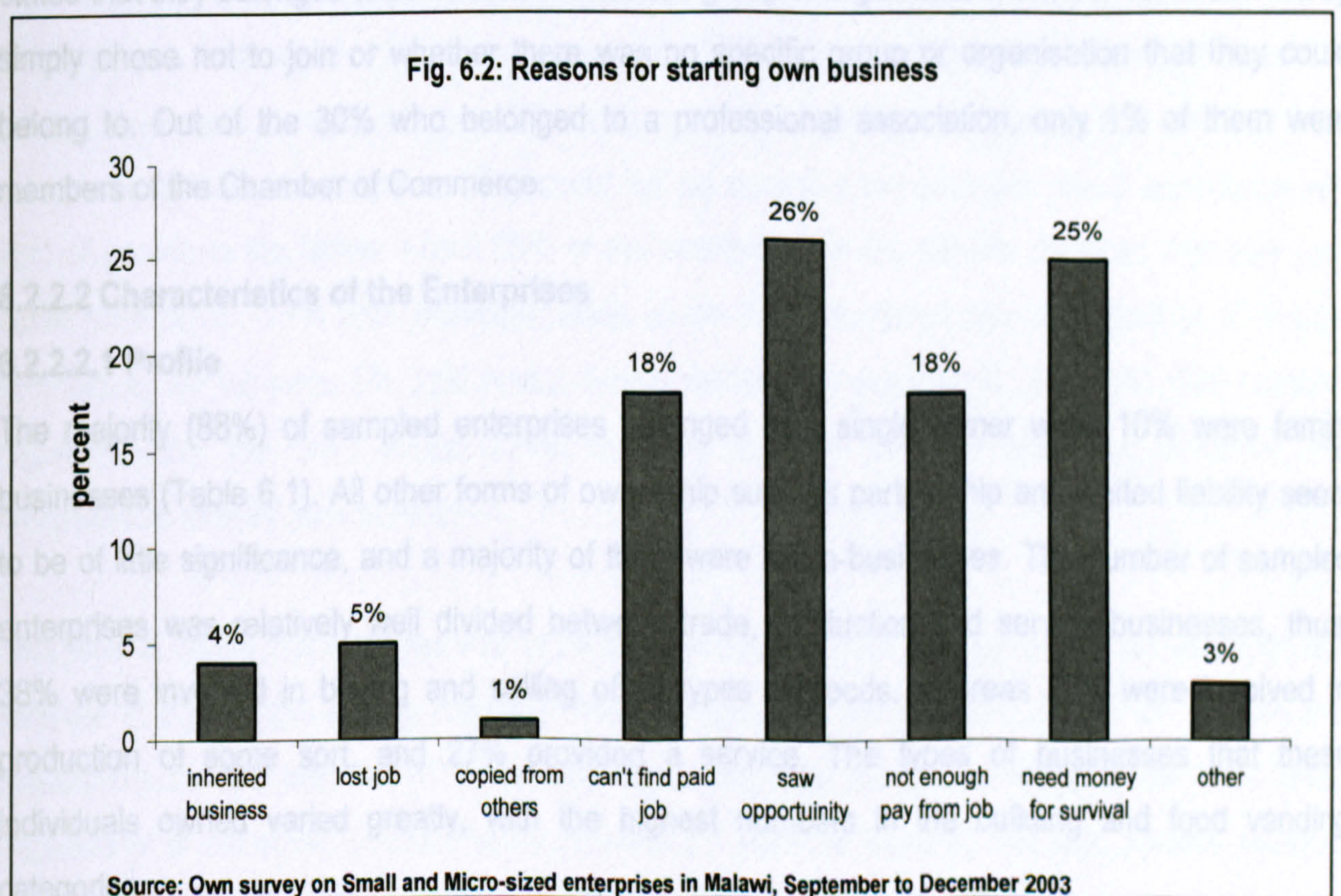
Lack of managerial know-how places significant constraints on SME development. Even though SMEs tend to attract motivated managers, they can hardly compete with larger firms. The scarcity of management talent, prevalent in most countries in the SSA region, has a magnified impact on SMEs. Despite the numerous institutions providing training and advisory services, there is still a



skills gap among the SME sector as a whole. According to Daniels and Ngwira (1993), about 88% of Malawian SMEs desired training in various skills but as of 1992, less than 6% had actually received it, and this survey has proven that this was still the case at the time of this study.

The survey results also indicated that there was a dominance of male entrepreneurs in the SME sector. Out of the individuals that were interviewed, 58% were male and 30% were female (Table 6.1), and in certain types of industries such as building contractors, mechanics, electricians, furniture and joinery, and plumbing the male dominance was total, as is usually the case in many parts of the world. However, it could be argued that the method for selecting the sample (purposive sampling and snowballing) might have had an influence on the sample composition. On the other hand it should be noted that even with this method of 'hunting' out entrepreneurs, the RA may have had come across more male than female entrepreneurs.

In addition to being self-employed in their business, around 30% of the entrepreneurs were also employed elsewhere. When asked why they started their own business, 26% said it was because they saw a demand opportunity while 25% said they needed money for survival (Figure 6.2), which could be characterised as 'subsistence' entrepreneurship.





The formal sector seems to have lost its attraction as a job avenue for the small-scale entrepreneur. Out of those who were not employed, asked if they were looking for paid employment, only 8% indicated that they were actively looking for a job and it seems reasonable to suggest that the small-scale sector provides an attractive job avenue.

Only 5% of the entrepreneurs said that they set up the business due to being retrenched from government. The majority of these individuals had never been civil servants, did not work in addition to running their own business and were not looking for any other type of employment instead of, or in addition to their own business. Those that indicated that they were looking for other employment, in addition to being self-employed, largely stated that they were doing so because the income they received from their own business was not enough for them to live on. The general non-hiring of labour by companies and state sector combined with the political freedom is encouraging more people to set up businesses. With job opportunities in the public sector decreasing and with the large-scale private sector trying to adjust to the structural adjustment programme, the alumni of the school system have now tended to set up small-scale enterprises, especially micro-firms and become self-employed.

Asked if they were a member of any business group/association, only 30% of the entrepreneurs stated that they belonged to some kind of business group or organisation, but it is not known if they simply chose not to join or whether there was no specific group or organisation that they could belong to. Out of the 30% who belonged to a professional association, only 1% of them were members of the Chamber of Commerce.

#### **6.2.2.2 Characteristics of the Enterprises**

##### **6.2.2.2.1 Profile**

The majority (88%) of sampled enterprises belonged to a single owner while 10% were family businesses (Table 6.1). All other forms of ownership such as partnership and limited liability seem to be of little significance, and a majority of them were micro-businesses. The number of sampled enterprises was relatively well divided between trade, production and service businesses, thus, 38% were involved in buying and selling of all types of goods, whereas 35% were involved in production of some sort, and 27% provided a service. The types of businesses that these individuals owned varied greatly, with the highest numbers in the building and food vending categories.



One way of assessing the effect of the SAPs on the character of the SME is the organisational birth rate of the small-scale enterprises. It appears that many of the individuals had not had their businesses for very long, with the largest majority of them having been created in or after 1994, thus, after democratisation of the country (Table 6.1). However, the fact that they were still around nearly 10 years later for some of them indicated that their businesses were doing relatively well. In general, over 90% of enterprises had been established since the inception of the SAPs and one of the main reasons cited by the entrepreneurs for starting a business during the mid-to-late 1990s was that they were given freedom, as a result of democracy, to carry out any business they liked without being intimidated by anybody as the situation was before the political changes. The following were the exact words of one entrepreneur, "we are now free to do business without any intimidation" and another, "there is no fear of political officials when carrying out a business". From these comments it appears that most of them associated mushrooming of SMEs in the mid-1990s to democracy rather than SAPs.

A large proportion of the sampled enterprises operated outside of the regulatory framework as over 70% of them were not registered with the government. 47% of them indicated that the reason for not registering was because their business was not big enough whilst the rest said they did not see the benefits of registering. One of the respondents even commented that, "registering is like exposing yourself to the government". Asked if they had any plans for registering in the future, 24% said yes they would, 17% were not sure and 59% gave an absolute 'no'. Some of those that did not have plans to register largely felt that they liked their business the way it was and that there was no need to register because they could not be sure that the business would experience any kind of growth in the future. About 65% of the enterprises in the sample declared that they paid some form of tax. 21% paid municipal taxes in the form of market fees and another 21% paid withholding tax whereas 5% paid surtax (Value Added Tax equivalent). Only 3% paid customs duties, notably the ones in the 21-50 category as they imported their raw materials and merchandise directly from abroad.

The general profile that emerged was of an informal micro-enterprise created in the mid-1990s and involved in buying and selling activities. This suggests that not necessarily SAP on its own was responsible for the creation of an environment conducive for mushrooming of informal SMEs (regardless of necessity or opportunity reasons for entrepreneurship) but also political freedom contributed to the situation.



#### **6.2.2.2 Procurement of raw materials**

Only 12% of the enterprises imported their raw materials or finished products, whereas over 80% procured these materials entirely from the local market. Enterprises in the clothing/tailoring sub-sector relied on imports especially: thus, 27% of enterprises in this sub-sector imported clothes/materials from neighbouring countries, notably from South Africa and Tanzania. The enterprises that purchased from other countries said it was because they found that this was cheaper than buying things from their home country and therefore they could keep their prices lower and still make a profit. Even with currency devaluations in Malawi, people were still buying goods from other countries and it is probably cheaper to do so due to high inflation rates in the country.

Inter-industrial relations were not very extensive: only 9% of the enterprises declared that they procured their raw materials from other enterprises in the local area. Inter-industrial exchanges took place in the food and woven products sub-sectors. Those that did not deal with other SMEs cited that not only did they not know them well enough, but also that there was a certain lack of trust among the small businesses. In fact, many interviewees emphasised the disadvantages of co-operative disposition, like jealousy, conflict and haggling on prices. They neglected the positive effects of strong co-operative links such as ready availability of special inputs or services, more rapid learning processes and increased competitiveness through concentration on core competences. This is supported by findings from industrial economics that the density of externalities is a key factor in explaining innovative capacity and competitiveness (OECD 1992).

#### **6.2.2.3 Markets supplied**

Table 6.2 gives a summary of information collected from the enterprises with regard to the type of customers supplied. Other SMEs were quite often cited as the most frequent customers of these businesses, but other SMEs were also seen to be their main competition, providing an interesting conundrum for many business owners. For enterprises in the sample as a whole, the main clientele was made up of other SMEs (33% of the enterprises), both rural and urban populations (27% of the enterprises) and low income urban populations (17% of the enterprises). As the size of the enterprise grew, the markets supplied moved from low-income populations to more captive markets, such as other SMEs, high-income population and larger companies, which are more demanding in terms of the quality of the products. None of the size 21 - 50 enterprises sold their products to rural or low-income urban populations. In comparison to older ones, the enterprises created since 1994 addressed a larger proportion of both rural and urban populations. Most of the businesses included in the survey, irrespective of their size, were mainly trading within their local



area, thus 97% declared that they sold their products within their district area. Very few enterprises exported, only 3% of the enterprises, including some micro-enterprises. Most of the exporting enterprises were in the wood products/furniture sub-sector. Enterprises created between 1988 and 1994 were the most likely exporters.

**Table 6.2: Main clientele by sub-sector of activity, size of enterprise and number of enterprises created in each year group (%)**

	MAIN CLIENTELE										
	Total	Rural Population	Low-income Urban population	High-income Urban Population	Both rural and urban Population	Large companies	Tourists	Vendors /Traders	Stalls and shops	Other SMEs	Other
<b>Branches of Activity:</b>											
Food products	26.5	5.1	33.3	0.0	30.8	0.0	0.0	7.7	0.0	20.5	2.6
Building & Construction	4.9	0.0	0.0	14.2	28.6	28.6	0.0	0.0	0.0	28.6	0.0
Construction materials	2.7	0.0	0.0	25.0	25.0	0.0	0.0	0.0	0.0	50.0	0.0
Wood products/furniture	10.2	13.3	6.7	6.7	13.3	0.0	13.3	0.0	0.0	46.7	0.0
Metal products	4.0	16.7	0.0	16.7	16.7	0.0	0.0	0.0	16.7	33.2	0.0
Clothing/tailoring	10.2	0.0	20.0	33.3	26.7	0.0	0.0	0.0	0.0	20.0	0.0
Woven products	2.7	0.0	0.0	25.0	0.0	0.0	0.0	0.0	25.0	50.0	0.0
Services	25.9	5.2	15.8	13.2	31.6	0.0	0.0	0.0	2.6	31.6	0.0
Shops/Stalls	2.7	0.0	25.0	0.0	50.0	0.0	0.0	0.0	0.0	25.0	0.0
Miscellaneous industries	10.2	6.7	6.7	0.0	20.0	0.0	0.0	0.0	0.0	66.6	0.0
<b>Size of enterprise:</b>											
Micro (1-4)	63.3	5.3	21.5	10.8	26.9	0.0	2.2	3.2	3.2	26.9	0.0
Small: (5-20)	32.6	8.3	10.6	8.3	25.0	2.0	0.0	0.0	0.0	45.8	0.0
(21-50)	4.1	0.0	0.0	16.7	33.3	16.7	0.0	0.0	0.0	33.3	0.0
<b>Enterprises Created:</b>											
Before 1981	4.0	16.6	0.0	0.0	16.7	0.0	0.0	0.0	16.7	50.0	0.0
Between 1981 & 1988	10.9	6.2	31.3	6.2	18.8	0.0	6.2	0.0	0.0	31.3	0.0
Between 1988 & 1994	32.0	8.5	6.5	12.8	21.3	2.1	2.1	4.2	2.1	40.4	0.0
After 1994	53.1	2.6	21.9	10.2	32.2	1.2	0.0	1.2	1.2	28.3	1.2
<b>Total</b>	<b>100.0</b>	<b>5.4</b>	<b>17.0</b>	<b>10.2</b>	<b>26.6</b>	<b>1.4</b>	<b>1.4</b>	<b>2.0</b>	<b>2.0</b>	<b>33.3</b>	<b>0.7</b>

Source: Own survey on Small and Micro-sized enterprises in Malawi, September to December 2003



As discussed elsewhere, Malawi's internal market is very small and this is compounded by the fact that income per head is one of the lowest in world. Transport and communication system within the country itself is very poor. Simply removing tariff barriers to trade will not make much difference to the local producers in terms of increasing market share through global integration since there are still these other non-tariff barriers to overcome yet. As seen here, even with all the trade reforms which have taken place in the country, a majority of the SMEs have local people as their main customers. The Malawi situation supports Sutcliffe's argument, discussed in section 2.5.2.1, that most SMEs rely on niche markets for their sustainability (Sutcliffe 1971).

Some may argue that trade reform measures may have little effect on SMEs since most serve local market niches, but as discussed in section 4.5.1.5 the SMEs have been affected by such policies as price deregulation, currency devaluation which affect prices of goods and drop in real wages affecting demand. Furthermore, the SMEs, like any other businesses need a stable economic environment to operate effectively, and one of the main SAP's objectives was to create a stable macroeconomic environment.

#### **6.2.2.2.4 Marketing and Competition**

Only 13% of the individuals from the survey indicated that the market supplied was not enough (Table 6.3). This is not surprising considering that most SMEs are rural-based hence the population they mostly supply is the rural. With high transport costs, most rural people cannot afford transport fares to go into the town centres to purchase their needs therefore they rely on the rural SMEs for their supplies.

For countries with a poorly developed transport and communication system like Malawi, it seems that small producers have established themselves in the local markets, which implies that they may need to compete with one another on the basis of products which suit the needs of local people. Since the market is already segmented by inadequate transport and communication system, the SMEs may have gained a larger relative role in their local markets and this supports Staley and Morse's argument that the local SMEs should be able to withstand competition from distant firms, even national ones, as they cannot easily penetrate the local markets due to transport barriers, and also that the products the SMEs supply are favoured and readily available for the local market (Staley and Morse 1965).



**Table 6.3: Main competitors by sub-sector of activity, size of enterprise and number of enterprises created in each year group (%)**

	MAIN COMPETITORS							MARKET SIZE		
	Total	Other SMEs	Large Enterprises	Both small and large Enterprises	Imports	Other competitors	None	More than enough	About right	Not enough
<b>Branches of Activity:</b>										
Food products	26.5	84.6	2.6	12.8	0.0	0.0	0.0	25.6	64.1	10.3
Building & Construction	4.9	0.0	14.3	85.7	0.0	0.0	0.0	71.4	28.6	0.0
Construction materials	2.7	25.0	25.0	50.0	0.0	0.0	0.0	75.0	25.0	0.0
Wood products/furniture	10.2	33.3	0.0	40.0	6.7	6.7	13.3	13.3	60.0	26.7
Metal products	4.0	83.3	0.0	16.7	0.0	0.0	0.0	16.7	83.3	0.0
Clothing/tailoring	10.2	46.7	13.3	26.7	0.0	0.0	13.3	40.0	46.7	13.3
Woven products	2.7	50.0	0.0	50.0	0.0	0.0	0.0	0.0	75.0	25.0
Services	25.9	52.6	0.0	42.1	0.0	2.6	2.7	36.8	50.0	13.2
Shops/Stalls	2.7	0.0	0.0	75.0	0.0	0.0	25.0	25.0	75.0	0.0
Miscellaneous industries	10.2	73.3	0.0	13.3	0.0	0.0	13.4	13.3	66.7	20.0
<b>Size of enterprise:</b>										
Micro (1-4)	63.3	69.9	4.3	19.4	1.0	0.0	5.4	24.7	62.4	12.9
Small: (5-20)	32.6	39.6	2.1	47.9	0.0	0.0	6.2	35.4	50.0	14.6
(21-50)	4.1	0.0	0.0	100.0	0.0	0.0	0.0	66.7	33.3	0.0
<b>Enterprises Created:</b>										
Before 1981	4.0	66.7	0.0	33.3	0.0	0.0	0.0	16.7	33.3	50.0
Between 1981 & 1988	10.9	56.3	0.0	43.7	0.0	0.0	0.0	31.2	68.8	0.0
Between 1988 & 1994	32.0	55.3	2.1	31.9	2.1	2.1	6.5	31.9	57.4	10.7
After 1994	53.1	57.7	5.1	29.5	0.0	1.3	6.4	29.5	56.4	14.1
<b>Total</b>	<b>100.0</b>	<b>57.1</b>	<b>3.4</b>	<b>32.0</b>	<b>0.7</b>	<b>5.4</b>	<b>1.4</b>	<b>29.9</b>	<b>57.2</b>	<b>12.9</b>

Source: Own survey on Small and Micro-sized enterprises in Malawi, September to December 2003

The data also revealed that the larger the enterprise, the less the competition from smaller units. The results showed that competition between small and large enterprises was weak: only 4.3% of micro and 2.1% of small enterprises mentioned large local enterprises as the main source of competition. Most of the competition experienced by the building and construction sub-sector came from both small and large enterprises (85.7%). Food products (84.6%) and metal products (83.3%)



got most of their competition from other SMEs. Enterprises created before 1981 experienced most competition (66.7%) from other SMEs.

Although competition was most felt in building and construction and metal products sectors, none of the interviewed entrepreneurs in these categories indicated that the market was not enough. Even in the food products sector, where competition is also intense, only 13% of them said that the market was not enough. Most entrepreneurs who said the market was not enough were from the wood products/furniture (27%) and woven products (25%). This may be one of the sub-sectors where production for export to foreign markets needs to be encouraged by the government and other support institutions. Export-led growth dates back to the years when wealth creation for nations was the way for economic development of countries. If these sub-sectors were given the opportunity to produce for domestic as well as foreign markets then market size would not be a major issue as export markets permit manufacturers to produce more of any single item hence specialise more than if they produced for the home market alone. It has also been argued that when export markets exist, labour, capital and even land can be moved rapidly from low to high-productivity uses without encountering diminishing returns (Behrman and Srinivasan 1995).

Half of those enterprises created before 1981 said that the market supplied was not enough. But then again it goes back to the same problems of accessing foreign markets and how to market their products in the international markets. Many of them may run into significant problems due to common pitfalls such as poor market analysis, poor understanding of competitive conditions in foreign markets, a failure to customise the product to the needs of foreign customers and lack of effective distribution programme, all of which the SAP should have taken into account in during the design stages.

### **6.2.2.3 Business Operating Environment**

The environment, be it economic, regulation, policies or physical, in which businesses operate play an important part in their performance, survival and development. Despite the wide-ranging economic reforms instituted in Malawi, SMEs still face a variety of constraints. The following sections discuss how the adjustment policies have affected SME operations in Malawi.

#### **6.2.2.3.1 Main problems and impact of Adjustment**

In the survey, entrepreneurs were asked to specify the main difficulties encountered in everyday operations of their business. The results are presented in Table 6.4. For the sample as a whole, the



three main problems mentioned most were: difficulty in obtaining capital for business growth (55%); high inflation rate (49%); and high taxes and duties (39%).

**Table 6.4 Main difficulties in everyday operations by size of the enterprise (%)**

	% of responses	Rank	Micro-enterprises (1-4)	Small-size enterprises	
				5 - 20	21 - 50
<b>Business environment</b>					
Taxes and duties	38.8	3	21.5	52.1	100.0
Bribery and corruption	8.8	8	8.6	8.3	16.7
Rent on premises too high	4.8	11	4.3	6.3	0.0
Not enough space in the market	2.7	14	2.2	4.2	0.0
Vandals and lack of security	1.4	16	0.0	4.2	0.0
<b>Machines and equipment</b>					
Expensive	5.4	10	6.5	4.2	0.0
Inadequate	4.8	11	5.4	4.2	0.0
Obsolete	1.4	16	1.1	2.1	0.0
<b>Finance</b>					
Difficulty in obtaining capital for growth	55.1	1	58.1	50.0	16.7
Difficulty in obtaining a loan	6.1	9	6.5	6.3	0.0
High interest rates affecting borrowing	4.1	12	6.5	0.0	0.0
Working capital tied up in clients	1.4	16	1.1	2.1	0.0
Working capital used up for living expenses	1.4	16	2.2	0.0	0.0
Long process for loan applications	0.7	17	2.1	0.0	0.0
<b>Demand</b>					
Too many similar SMEs in the same sector	14.3	6	17.2	10.4	0.0
Not enough money income in general	5.4	10	4.3	8.3	0.0
Small market size	3.4	13	4.3	6.3	0.0
Competition from cheaper imports	0.7	17	1.1	0.0	0.0
<b>Procurement of raw materials</b>					
High inflation rate affecting cost of inputs	48.9	2	48.4	50.0	50.0
Frequent currency devaluation	24.5	5	27.9	14.6	50.0
Scarcity of raw materials	5.4	10	3.2	8.3	16.7
Where we procure raw materials very far	3.4	13	5.4	0.0	0.0
Price of materials too high	1.4	16	0.0	4.2	0.0
<b>Employees</b>					
Unskilled and untrained employees	2.0	15	2.2	2.1	0.0
Not enough workers	1.4	16	2.2	0.0	0.0
High employee turnover	1.4	16	0.0	4.2	0.0
<b>Infrastructures</b>					
High cost of transport due to high fuel cost	31.9	4	32.3	33.3	16.7
Frequent electricity power cuts	2.0	15	2.2	2.1	0.0
Other difficulties	10.2	7	9.7	12.5	0.0

Source: Own survey on Small and Micro-sized enterprises in Malawi, September to December 2003

Access to finance, in terms of obtaining capital for growth and obtaining credit, was a dominant constraint to SMEs in Malawi. This stems from the fact that SMEs have limited access to capital markets, locally and internationally, in part because of the perception of higher risk, informational barriers, and the higher costs of intermediation for smaller firms. As a result, SMEs often cannot obtain long-term finance in the form of debt and equity. Not being able to obtain capital for business growth was mentioned particularly by micro-enterprises as the main difficulty (58%). The main problems listed by the micro-enterprises give a good indication of the limits of their growth potential, which is restricted by the conjunction of two constraints: a finance constraint (lack of capital for



growth) and a raw materials constraint (high inflation rate affecting cost of materials). This indicates that they operate in an unstable economic environment.

The small-sized enterprises are also sensitive to difficulties which restrict the procurement of raw materials. A high inflation rate, which was as high as 83% in 1995 (Table 4.6) and, although, it went down to around 10% in 2003 (Table 4.7), still constituted the main problem affecting purchase of raw materials. Most of the small-sized enterprises mentioned this problem, which ranked second to taxation (Table 6.4). A comment made by one of the entrepreneurs was that, "high inflation rate is preventing me from buying other input materials which would be beneficial to the business". The SMEs emphasised high inflation and currency devaluation as affecting the procurement of raw materials. Although not pointed out by the entrepreneurs themselves, the problems with cost of raw materials may also stem from poor cash flows (Parker et al, 1995), because as also indicated in the data some of them had mentioned cash tied in with creditors as a constraint. The high price of raw materials was, surprisingly, not a big constraint and ranked 16<sup>th</sup> amongst the SMEs.

Nearly 40% of the SMEs mentioned tax and duty as one of the major constraints to their operations. High taxation came at the top of the list for the problems mentioned by most small-sized enterprises. The micro-enterprises are penalised by the level of taxation which affect them all the more, since the tax they had to pay was a fixed regardless of amount of profit made. The SMEs felt that the level of taxation was high relative to their profits.

From the comments made by the entrepreneurs, the level of taxation and difficulties in gaining access to credit were the major obstacles to continuing structural adjustment of the industrial sector. The entrepreneurs expressed that they would have liked the authorities to relax taxation and use a less coercive policy with regard to overdue payment penalties. Simplifying taxation was also very much desired by some entrepreneurs who complained about the increase in number of different taxes and who would have preferred that the authorities removed some of the taxes or merged them into one single tax.

In terms of high transport costs, infrastructural problems ranked 4<sup>th</sup> as a constraint for the SME business operations. This is not surprising as high inflation and low value of the Malawi currency result in expensive petroleum and fuel imports which later impacts on SME operating costs. Poor road network and maintenance also make transport cost relatively expensive for SMEs because transporters usually charge more when the roads are poorly maintained and if links between areas



are not direct. This impacts on the SMEs by restricting them to the local markets and by raising the cost of purchasing input materials from outside their own local areas.

Employee problems seemed a less important constraint to SMEs in Malawi. SMEs generally use simple technology which does not require highly skilled workers. However, where skilled workers are required, an insufficient supply of skilled workers can limit the specialisation opportunities, raise costs, and reduce flexibility in managing operations. The survey found that only 2% of the respondents indicated that they found skilled labour to be a constraint. With regard to machinery and equipment problems, only 1% of the sampled firms mentioned old equipment as one of the constraints to business operations and only 5% said equipment was expensive. It is common knowledge that most SMEs have difficulties in gaining access to appropriate technologies and information on available techniques, and this limits innovation and SME competitiveness. Besides, other constraints on capital, and labour, as well as uncertainty surrounding new technologies, lack of appropriate technology restricts incentives to innovation. Contrary to this, the Malawi SMEs did not rank this as one of the top constraint probably because most of their operations are labour-intensive and trading activities.

Competition for customers and markets ranked 6<sup>th</sup> as a constraint. Although, recent economic policies have led to a decline in the role of the state in productive activity, and a renewed private investment has created new opportunities for SMEs, limited access to public contracts and subcontracts, arising from cumbersome bidding procedures and/or lack of information, inhibit SME participation in other domestic markets in the country. Inefficient distribution channels often dominated by larger firms also pose important limitations to SMEs to expand to other areas/markets in the country.

The dismantling of protectionist barriers introduced as part of the SAPs was not seen as a problem for the surveyed enterprises. Although the SMEs had problems with competition from other similar SMEs, they did not view competition from cheaper imports as a major constraint. Only around 1% of all the enterprises mentioned competition from imports as a main problem, in fact this ranked last on the list. This is contrary to the responses from government officers who expressed concerns over Malawi being flooded by imports. From the government's point of view too many imports is not conducive to economic growth. However, from the entrepreneurial point of view, it is expected that they would not see competition from imports as much of a problem since for most of them buying and selling of imports is their main entrepreneurial activity, and most of the goods they buy are from



other countries anyway. From the results in Table 6.4, it can also be seen that bribery and corruption ranked eighth in the difficulties the SMEs faced in the operating environment. The following is an example of the typical statements made: "top government officials are oppressing us, they are probably more interested in developing themselves rather than concerned about poverty alleviation".

The analysis of the response of the SME sector to the SAPs is complex because it is subject to several, often-conflicting forces, the relative importance of which depends on the measures taken. An evaluation of the impact of SAPs was dealt with by asking the entrepreneurs to describe the main changes recorded since trade reforms in terms of production, employment, investment, product range, exports and imports. The results are presented in Tables 6.5, 6.6a, 6.6b and 6.7 and discussed in the following sections.

#### 6.2.2.3.2. Impact on production and employment

Table 6.5 presents side by side the results of the survey on the evolution of production and employment since 1981. As mentioned earlier, the firms were subdivided by size and period of creation to better assess their behaviour since the reforms were established. This was to find out the reaction of the SMEs to the incentive mechanisms set up and if their production and employment grew.

Table 6.5 Impact of the adjustment on production and employment by size of enterprise and year of creation (%)								
			Production		Employment			
			Increase	Decrease	Increase	Decrease	No change	
Period of creation	Size	Total						
Before 1981	Micro	(1 – 4)	2.0	0.0	100.0	16.7	0.0	33.3
	Small	(5 – 20)	2.0	0.0	100.0	100.0	0.0	0.0
		(21- 50)	0.0	0.0	0.0	0.0	0.0	0.0
Between 1981 and 1988	Micro	(1 – 4)	6.1	11.1	88.9	33.3	0.0	66.7
	Small	(5 – 20)	4.8	28.6	71.4	85.7	14.3	0.0
		(21- 50)	0.0	0.0	0.0	0.0	0.0	0.0
Between 1988 and 1994	Micro	(1 – 4)	16.4	16.7	83.3	28.0	0.0	72.0
	Small	(5 – 20)	13.6	26.3	73.7	75.0	10.0	15.0
		(21- 50)	2.0	0.0	100.0	50.0	0.0	50.0
After 1994	Micro	(1 – 4)	38.8	17.9	82.1	17.5	1.8	80.7
	Small	(5 – 20)	12.3	22.2	77.8	77.8	5.6	16.6
		(21- 50)	2.0	33.3	66.7	33.3	33.3	33.3
Total			100.0	18.4	81.6	41.5	4.1	54.4
Source: Own survey on Small and Micro-sized enterprises in Malawi, September to December 2003								



Entrepreneurs were asked to describe changes in production since the start of their businesses, and, for the sample as a whole, a large proportion (82%) of them declared that their production had decreased. Since most of the enterprises were created after 1988 (when most policies affecting industry and SMEs were implemented), with a majority created after 1994, it is difficult to tell for sure whether the decrease in production was due to SAPs or some other factors. However, irrespective of the size and the period in which they were established, the decrease affected all enterprises unilaterally.

Another observation from Table 6.5 is that the proportion of enterprises that declared to have had a decrease in production was particularly high (100%) for enterprises established before 1981, which may indicate that these enterprises reacted negatively to incentive measures taken. It is possible that these results show the effects of a negative response of supply to the adjustment measures. This consideration must be counterweighted, however, by the fact that the Malawi economy is sensitive to changes in weather and that the 1980s were characterised by a record decline in agricultural growth, which spread to the entire economy. In other words, for lack of more specific indications, the decline phenomenon observed in the sample of enterprises may be due exclusively to the trend of the markets. The small enterprises recorded the largest rise in employment (Table 6.5). The shrinking formal labour market increased the flow of jobless people who tried to generate an income by establishing small businesses. Employment grew the least in micro-enterprises. The weak entry and exit barriers are such that there are as many micro-enterprises leaving the market as new ones being established, thus causing stagnation of employment.

Table 6.6a shows out of all the sampled enterprises, only 18% had increased production and 42% had increased employment. 75% of those in groceries/hawkers had increased their supplies and 33% SMEs in clothing and tailoring had increased production. All of the metal and woven products SMEs recorded a decrease in production. 75% of construction materials and 67% of metal products SMEs said they had increased employment.

As mentioned before it is difficult to ascertain whether the changes noticed by the entrepreneurs were due to SAPs or some other factors. The analysis of the impact of SAPs on SMEs is made more complex by the fact that most of the surveyed SMEs were created after 1988 when trade reform policies were first implemented and an even larger number of them were created after 1994 when the country underwent the political changes. However, it should be noted that these results are what the entrepreneurs observed as changes either since the start of their business or since



the trade reform measures. The main responses which came out included currency devaluation, high inflation, taxes, all of which are issues related to the reform measures.

**Table 6.6a: Impact of the adjustment on production and employment by sub-sector of activity (%)**

<i>Sub-sector of activity</i>		Production		Employment		No change
		Increase	Decrease	Increase	Decrease	
Enterprises Total %	100.0	18.4	81.6	41.5	4.1	54.4
Food products	26.5	15.4	84.6	30.8	0.0	69.2
Building/Construction	4.9	14.3	85.7	57.1	14.3	28.6
Construction materials	2.7	25.0	75.0	75.0	0.0	25.0
Wood products/furniture	10.2	6.7	93.3	33.3	13.4	53.3
Metal products	4.0	0.0	100.0	66.7	0.0	33.3
Clothing/Tailoring	10.2	33.3	66.7	26.6	6.7	66.7
Woven products	2.7	0.0	100.0	25.0	0.0	75.0
Services	25.9	21.1	78.9	60.5	5.3	34.2
Groceries/Hawkers	2.7	75.0	25.0	50.0	0.0	50.0
Miscellaneous	10.2	13.3	86.7	20.0	0.0	80.0

Source: Own survey on Small and Micro-sized enterprises in Malawi, September to December 2003

The changes observed could have been a result of many different factors or a combination including drought, lack of business management skills by owners, poor infrastructure. But then again, one may argue that issues like training, infrastructure should have been incorporated within the SAP in the first place. The fact that the issues were underestimated or overlooked to begin with whilst the policies concentrated in other areas, makes the SAPs even more to blame when the SME performance is negative.

#### 6.2.2.3.3 Impact on investment

Most entrepreneurs said that they had not purchased any new equipment recently or modernised their production in any way due to lack of money. Only around 40% of all the enterprises questioned declared that they had made new investments in the form of purchase of equipment. All of the construction-materials enterprises indicated that they had invested in new equipment, and none of the enterprises in woven products sub-sector had done so (Table 6.6b). Although a high proportion of the building, construction materials and metal-production sub-sector enterprises had invested in new equipment, they did not benefit much from this capitalisation effort as this is not reflected in the increased production results (Tables 6.6a).



**Table 6.6b: Impact of the adjustment by sub-sector of activity (%)**

<i>Sub-sector of Activity</i>	<i>Total %</i>	<i>Food Products</i>	<i>Building/ Construction</i>	<i>Construction materials</i>	<i>Wood products/ furniture</i>	<i>Metal products</i>	<i>Clothing/ Tailoring</i>	<i>Woven Products</i>	<i>Services</i>	<i>Groceries/ Hawkers</i>	<i>Miscellaneous</i>
Total %	100.0	26.5	4.9	2.7	10.2	4.0	10.2	2.7	25.9	2.7	10.2
Purchase of new equipment	40.1	33.3	85.7	100.0	33.3	83.3	40.0	0.0	47.4	25.0	6.7
Change in product range	17.0	10.3	28.6	25.0	33.3	33.3	20.0	75.0	7.9	0.0	13.3
Accessing foreign markets	2.7	0.0	14.3	0.0	13.3	16.7	0.0	0.0	0.0	0.0	0.0
Share of imported raw materials: Currently import	12.9	2.6	14.3	25.0	13.3	16.7	26.7	0.0	13.2	0.0	26.7
Increased	26.3	100.0	0.0	0.0	50.0	0.0	0.0	0.0	40.0	0.0	25.0
Decreased	26.3	0.0	100.0	0.0	0.0	0.0	50.0	0.0	40.0	0.0	0.0
No change	47.4	0.0	0.0	100.0	50.0	100.0	50.0	0.0	20.0	0.0	75.0
Difficulty in obtaining raw materials	29.3	33.3	0.0	0.0	33.3	33.3	26.7	50.0	34.2	50.0	13.3
Change in customer numbers: Increased	21.1	28.2	0.0	75.0	6.7	16.7	6.7	0.0	26.3	25.0	20.0
Decreased	25.9	23.1	42.9	0.0	46.7	16.7	26.6	25.0	23.7	50.0	20.0
No change	53.1	48.7	57.1	25.0	46.7	66.7	66.7	75.0	50.0	25.0	60.0
Product competitiveness Domestic market	77.6	94.9	100.0	100.0	100.0	100.0	93.3	75.0	52.6	100.0	26.7
International	48.9	64.1	57.1	75.0	73.3	66.7	46.7	50.0	26.3	75.0	20.0
Exporting enterprises	2.7	0.0	14.3	0.0	13.3	16.7	0.0	0.0	0.0	0.0	0.0
Enterprises who would like to export	26.5	33.3	28.6	0.0	40.0	0.0	40.0	50.0	15.8	75.0	6.7
Supply constraints: Enterprises able to sell more	78.2	79.5	100.0	50.0	73.3	83.3	93.3	100.0	76.3	75.0	60.0
Demand constraints: Enterprises able to sell current levels but no more	87.1	89.7	100.0	100.0	73.3	100.0	86.7	75.0	86.8	100.0	80.0
Enterprises not able to sell current production	12.9	10.3	0.0	0.0	26.7	0.0	13.3	25.0	13.2	0.0	20.0

Source: Own survey on Small and Micro-sized enterprises in Malawi, September to December 2003



Purchase of new equipment was mostly made by the 5-20 and 21-50 employee-size enterprises (Table 6.7). Enterprises created before 1988 were more likely to modernise their means of production than those established after 1994. Over half of them declared that they had acquired new equipment since trade liberalisation compared with 36% of those established after 1994. These results suggest that the enterprises reacted to the rise in production by making new investments. They also shows that an effort was made to adapt to the new economic environment by enterprises which formerly benefited from strong protection.

#### **6.2.2.3.4 Impact on products and markets**

The investment effort made by enterprises did not result in a notable change in the range of products. Only 17% of all the enterprises declared that they had modified their range of products, and three-quarters out of woven products enterprises, 33% out of wood products and 33% out of metal products enterprises had made these changes (Table 6.6b). Not many enterprises within the food products, services and groceries/hawker sub-sectors had made changes to their product range. In fact, these branches of activities are less vulnerable to competition from imported products, either because they are standardised (groceries/hawkers) or because they correspond to the specific tastes of the market supplied (food products). Only 2.7% of all the enterprises claimed that they had penetrated foreign markets, something which mostly happened within building/construction, wood and metal production sub-sectors (Table 6.6b), and 21-50 size enterprises (Table 6.7).

#### **6.2.2.3.5 Impact on exports**

Increasing the export of manufactured products was generally one of the objectives sought by the structural adjustment programme as the domestic market is too small to support the growth of the industrial sector on its own. Malawi is a weak exporter of manufactured products and this was confirmed by the survey results. Surprisingly, sampled enterprises in the food-products sector did not export at all, and only 33% of them expressed the interest to export directly (Table 6.6b). None of the woven products, clothing or construction materials were being exported. However, enterprises in the wood, woven products and clothing were amongst those who expressed interest in exporting in future (Table 6.6b). Overall, 27% envisage producing for export, with only 32% out of the owners of micro enterprises and one-third of the 21-50 size enterprises (Table 6.7). The lack of knowledge of markets and export channels, and above all the difficulty in obtaining credit to produce for export, were the main difficulties noted. Also it could be due to the fact that most of the sampled enterprises had small numbers of staff, who lacked training in business skills, and therefore were not capable of dealing with processes and procedures involved with the exporting



activity. Most of the enterprises did not export their products either because of the cost or the lack of understanding of how to do so, and they also indicated that they would not be interested in exporting their products even if they could.

**Table 6.7 Impact of the adjustment by size of the enterprise (%)**

	Total %	Micro-enterprises (1-4)	Small-size enterprises	
			5 - 20	21 - 50
Total %	100.0	63.3	32.6	4.1
Purchase of new equipment	40.1	22.6	68.8	83.3
Change in product range	17.0	15.1	18.8	33.3
Accessing foreign markets	2.7	2.2	2.1	16.7
Share of imported raw materials: current	12.9	9.7	18.8	16.7
increased since trade liberalisation	26.3	22.2	33.3	0.0
decreased since trade liberalisation	26.3	33.3	11.1	100.0
no change	47.4	44.5	55.6	0.0
Difficulty in obtaining raw materials	29.3	28.0	35.4	0.0
Difficulty in obtaining credit	85.0	89.2	83.3	33.3
Changes in customer numbers				
increased	21.1	20.4	25.0	0.0
decreased	25.9	22.6	29.2	50.0
no change	53.1	57.0	45.8	50.0
Product competitiveness on:				
domestic market	77.6	80.6	68.8	100.0
international market	48.9	52.7	41.7	50.0
Exporting enterprises	2.7	2.2	2.1	16.7
Enterprises who would like to export	26.5	32.3	14.6	33.3
Supply constraints				
enterprises able to sell more	78.2	74.2	83.3	100.0
Demand constraints				
enterprises able to sell current production but not more	87.1	87.1	85.4	100.0
not able to sell current production	12.9	12.9	14.6	0.0

Source: Own survey on Small and Micro-sized enterprises in Malawi, September to December 2003

These findings suggest that exporting remains a difficult challenge for many enterprises. Whereas large multinational enterprises have long been conversant with the steps that must be taken to export successfully, small enterprises can find the process intimidating. While large enterprises tend to be proactive about seeking opportunities for profitable exports, many small ones are reactive. Typically they would not consider exporting until their domestic market is saturated to force them to look for growth opportunities in foreign markets. Furthermore many of them tend to wait for opportunities rather than going out to seek them. When opportunities arise, small



enterprises may not respond, either due to lack of finance for growth or the desire to export, as one entrepreneur said, "I am not interested in exporting".

Those who expressed an interest in exporting would need to become more proactive about seeking export opportunities. But they may be unfamiliar with foreign opportunities, as one entrepreneur said, "I don't know how to go about supplying larger enterprises in this country let alone how exporting works or where these foreign markets are". They do not appreciate the magnitude of export opportunities and how to access them. Potential exporters are often intimidated by the complexities and mechanics of exporting to countries where business practices, language, culture, legal systems and currency are all different from those in the home market. The enterprise wishing to export would have to identify foreign market opportunities, find ways of avoiding a host of unanticipated problems that are often associated with doing business in a foreign market, familiarise itself with the mechanics of export and import financing and learn how to deal with foreign exchange risks. It can therefore be argued that when SAP was being introduced, not much thought was given to the implications of the capabilities of SMEs to access and operate in foreign markets. Probably that is why Malawi is in a situation of having more goods and services coming in rather than going out. Foreign imports are fulfilling the domestic market demand, and the country's own manufacturers are unable to compete and supply foreign markets. If these results are a reflection of the true position of SMEs in Malawi, in terms of exporting, then it can be argued that SAP has failed one of its fundamental goals.

#### **6.2.2.3.6 Impact on imports**

With liberalisation of the purchase of foreign currency, enterprises from the industrial sector generally do not encounter problems in obtaining the necessary currencies to purchase imported inputs materials. From this standpoint, the adjustment should not have a significant effect on the imports for firms. However, the adjustment programme is accompanied by a liberalisation of exports and a realignment of customs duties to reduce differences between the rate on imports and the rate on finished products. The effect sought is to substitute products of local origin for imported raw materials. The survey shows that only around 13% of the surveyed SMEs were currently importing raw materials (Table 6.6b).

The food products sector had the largest number of enterprises which experienced a rise in the share of imported raw materials followed by the wood/furniture sector (50%) (Table 6.6b). Only enterprises in woven products sector declared that they did not use imported raw materials, and



this was due to a fall in activity within that sector rather than to the substitution of imports by local inputs. Overall, the adjustment seems to have given rise to the anticipated effects with regard to a more intensive use of local resources. However, the distinction between imported raw materials for producers and imported finished goods should be clarified. Most of the entrepreneurs would say that they do not import their goods as they buy supplies from other enterprises that import them or act as intermediaries. So, for the manufacturers it could be seen as if they are using local materials when in actual fact they are purchasing their inputs from somebody who is importing them. There are other possible interpretations for these findings. First, it is possible that with the deregulation of domestic prices the ratio of relative prices underwent a notable change in favour of local products. Secondly, it could be that the slight increase in imported inputs originates from the industrial structure in Malawi, thus, the price elasticity of domestic demand is limited by the absence of national substitutes for the imported products. Finally, the devaluation of the MK currency as compared to currencies of the countries supplying the raw materials may have made the real economic cost of imported inputs relatively more expensive.

The respondents cited currency devaluation as one of the top problems affecting SMEs even though not many of them imported directly or dealt with foreign exchange. Out of the 13% who were directly importing inputs and only a small proportion out of the micro-sized enterprises did so. One would assume that out of the surveyed activity sub-sectors, metal products, services and to some extent clothing (there is a big market for second-hand clothing in Malawi, which are mostly imported) would be top of the list of importers of raw materials. Malawi hardly produces its own metal hence any metal-related products means that at some point raw metal was imported by a wholesale company. Service industries such as private hospitals/clinics rely on imported medical products. Similarly, transport service rely on imported vehicles and parts. But the survey showed a less proportion of importers out of the services or metal products compared to construction materials which are naturally occurring in Malawi.

SME activities like construction materials, food products, wood and woven products are hardly expected to rely on imports as they use agricultural or naturally occurring inputs locally found in the country, with production usually on a small-scale to satisfy local markets. Therefore the SMEs in these activity sub-sectors would rarely deal with foreign exchange hence not directly affected by changes in currency value. However, some of the sectors indirectly buy and use imported inputs from wholesalers who are directly affected by the currency devaluations. For instance, in the food products sector, those rearing chickens have to rely on chicken feed and chicks imported, by



intermediary companies, from Zimbabwe and other African countries. Hence whatever effects and cost implications of currency devaluation which the wholesaler importers suffer, they are later transferred to their customers, who are mostly the small and micro-enterprises. Probably that is why some of the surveyed SMEs said that currency devaluations were a constraint to their operations, even though they did not deal in foreign exchange directly themselves.

#### **6.2.2.3.7 Impact on competition**

The adjustment was intended to stimulate both national and international competition by deregulating economic activity and liberalising commercial exchanges. At the beginning of adjustment, imports constituted the main threat to national enterprises, particularly for the large ones in the modern sector which operated in import-substitution markets. This scenario does not seem to apply very much in Malawi taking into account the survey results. Imports were cited by only 0.7% of the enterprises (Table 6.3) as the main source of competition. Only 1% of the micro enterprises felt threatened by the entry of competing foreign products and the small-sized enterprises were less sensitive to the intrusion of imported products. They operate on different markets and the competition from other small firms was what threatens their survival. In the words of one interviewee regarding competition amongst themselves, "there is too much competition in businesses these days and the market is very small". Again it can be argued here that it is expected that imports would not be cited as the main source of competition to the SMEs because most of them are engaged in buying and selling imported goods, hence what is happening is that SMEs are competing amongst themselves for the market share rather than offering differentiated or competitive products.

With regard to the products they offered, about 78% felt that their products were competitive on the domestic market whereas 49% said they thought their products would be competitive on international markets. Construction materials, groceries/hawker and wood/furniture production sectors were amongst the top sub-sectors who felt that they offered competitive products internationally. Least competitive were the clothing/tailoring and services sub-sectors (Table 6.6b). Micro-enterprises were the most (53%) firms who said that their products would be competitive on the international markets (Table 6.7). However, it should be noted that a higher proportion of the 5-20 and 21-50 enterprises thought they were internationally competitive than was the case for the 1-4 size enterprises. Again here, it raises the same question of whether they themselves manufactured the products they sell or whether they were from imports which would explain why they felt that whatever they were selling would be competitive on the international markets.



#### **6.2.2.3.8 Impact on viability**

The impact of adjustment on the viability of enterprises depends on the capacity of entrepreneurs to adjust to the new economic context based on greater competition and better access to external markets. Exporting enterprises are in a better position to take advantage of the new reforms, whereas import-substitution firms are affected negatively because their viability is directly threatened by the increased competition as a result of the elimination of quotas and the harmonisation of tariff protection. The data in the survey confirm this interpretation. In answer to the question of viability of their enterprise, 35% of the entrepreneurs declared that their enterprise was more profitable than before, which is not too bad considering that only 0.7% exported their products. The enterprises, which declared that they were more profitable, were essentially micro-enterprises in the services and food products sub-sectors. Enterprises established since 1994 were comparatively more profitable than those established before that year. The 21-50 category enterprises seemed particularly penalised by the adjustment measures as 83% of them declared that they were less profitable, confirming the vulnerability of import-substitution firms to changes in the economic rules of the game.

#### **6.2.2.3.9 Constraints with regard to continuation of the Adjustment**

Growth in demand is supposed to encourage firms to make the required investments to become more efficient and more competitive, which in turn brings about growth of production and employment. Tables 6.6b and 6.7 give a few indications as to the constraints of supply and demand as perceived by the entrepreneurs interviewed. The data in these tables indicate that the enterprises in the sample are not much restricted by low levels of local demand. Only 13% declared that they could not sell current production whereas the majority (87%) declared that they could sell current production. Not many of the enterprises seemed to have supply-related problems either: 78% of all enterprises at least sold their entire production and could even sell more, particularly firms in the building and construction, woven products and clothing/tailoring branches. The factors, which limited supply, were mainly the chronic insufficiency of working capital. The other factors which also had a negative effect on production capacity were: lack of storage infrastructure (damage of products, notably in the rainy season); fluctuation of prices of agricultural inputs, notably out of season; and deterioration or lack of transportation infrastructures hindering regular supply of raw materials. Many of the entrepreneurs used private mini-buses or their own personal vehicles to transport their goods and stated that transport cost was very high. The cost of fuel was largely to blame for high cost of transportation, as expressed by one interviewee: "transport cost is very high such that all profits are taken up by this". Supply of water and electricity, however, did not appear to be a big problem for most of them, although some had more difficulties with electricity



power cuts than with water. Since most SMEs are engaged in buying and selling of finished goods, water and electricity would not pose much of a problem for these types of activities.

#### 6.2.2.3.10 Financing enterprises and access to credit

Financial matters present the most acute problem for SMEs and formal financial institutions provide capital to SMEs only in the rarest of cases. Table 6.8 gives an overview of the information obtained from the entrepreneurs with regard to financing of their enterprises. In most cases, the main source of financing at the beginning of activities was loans or gifts from family and friends (40%) followed by personal savings at 18%. One of the main reasons for using their own funds was that they found it extremely difficult to get credit from lending institutions to start their businesses. As far as financing at the beginning of activities is concerned, only 7% of the surveyed enterprises had the benefit of receiving funds from a bank or a credit agency (Table 6.8). One interviewee made the following comment: "by not providing us with loans, they are hindering our businesses from growing".

**Table 6.8 Financing of enterprises and access to credit (%)**

	Total %	Micro-enterprises (1-4)	Small-size enterprises	
			5 - 20	21 - 50
Total %	100.0	63.3	32.6	4.1
Financing for establishing an enterprise (main source):				
Personal savings	18.4	22.6	12.5	0.0
Redundancy/retirement money	14.9	11.8	16.7	50.0
Loan or gift from relatives/friends	39.5	38.7	41.7	33.3
Inherited the business	4.8	3.2	8.3	0.0
Bank/Building society or agency loans	6.8	2.2	14.6	16.7
Other sources	15.6	21.5	6.2	0.0
Difficulty of obtaining funds for business growth:				
Very difficult	42.9	52.7	29.2	0.0
Quite difficult	12.9	11.8	14.6	16.7
Quite easy	35.4	25.8	50.0	66.6
Very easy	8.8	9.7	6.3	16.7
Difficulty of obtaining funds for financing new equipment:				
Very difficult	40.1	45.2	33.3	16.7
Quite difficult	15.6	13.9	20.9	0.0
No change	5.4	8.6	0.0	0.0
Quite easy	4.1	1.1	8.3	16.7
Very easy	30.0	25.8	33.3	66.6
Not sure	4.8	5.4	4.2	0.0
Difficulty of obtaining credit:				
Very difficult	67.3	72.0	64.6	16.7
Quite difficult	17.7	17.2	18.7	16.7
Quite easy	10.2	6.5	14.6	33.3
Very easy	4.8	4.3	2.1	33.3

Source: Own survey on Small and Micro-sized enterprises in Malawi, September to December 2003



The data confirms the conservative practice of the banking system both with regard to its willingness to finance industrial operations and with regard to the conditions of access to credit. They also show that despite the re-organisation of the banking system undertaken in the context of SAPs access to finance remains a major constraint for enterprises. Banks are less inclined to provide capital to set up a business, but are more willing to finance projects for expansion or working capital. This is evidenced by the fact that when they were asked how difficult or easy it was to obtain funds for business growth, around 44% said it was either quite easy or very easy. Less than 30% of the micro-sized enterprises found it quite easy and less than 10% found it very easy to obtain funds for growth from banks. Since the structural adjustment measures were taken, many entrepreneurs still found it difficult to obtain funds for purchasing new equipment, and this is particularly very difficult for micro-enterprises.

Despite the presence of multiple and often interrelated constraints such as inadequate infrastructure, high transport costs, legal and regulatory restrictions, the widespread belief, from most enterprise surveys, is that lack of working capital constitutes the main obstacle to SME performance. In this competitive age, once the business is up and running, SMEs have been suffering from insufficient orders, reduction in trade volumes and prolonged credit term for buyers. All these problems have in turn created cash flow problems for SMEs. At the same time, prevailing economic climate makes it difficult for SMEs to obtain loans from lending institutions to meet their operational needs. Since the enterprises are operating in increasingly competitive markets and are limited in their growth by the moderate demand in the market, they have serious difficulty in even finding funds for their working capital to finance their current operations: over 60% of the firms interviewed declared that they were in need of funds for working capital and expansion.

Although the financial market has been liberalised, the needs of SMEs are still not being satisfied due to limited access to both working capital and long-term credit. Banks and other lending institutions are reluctant because SMEs seem to have a history of bad credit with them. Despite this, the banking sector and other formal lenders still get the blame for not providing credit to SMEs. Failure of SME growth and development can not be blamed on financial institutions alone, but also on SME customers who fail to honour their credit. The problem of working capital being tied up with clients came up often in the interviews. One interviewee made the following comment: "I have customers who buy on credit and don't pay me back and some of them even pass away before they settle their credit, making it very difficult for businesses". It could therefore be argued that



some entrepreneurs are unable to make repayment on their loans to the formal lenders because their own finances are tied in with their own customers.

High interest rates and the banks' lack of interest in lending to those that did not already have a lot of cash in their bank account appeared to be the most serious problems when it came to getting money from lenders. Conditions for obtaining loans are so restrictive that nearly 70% of the enterprises considered it was useless to apply for a loan from a bank or other lending institutions, either because their guarantees were insufficient or because of the complexity of bank procedures or their own ignorance of these procedures.

It was also felt that there was a lot of corruption amongst the lending institutions. One interviewee went further to make the following comment: "certain people are given lower interest rate on loan than others by the same lenders". The entrepreneurs indicated that they would like to see an end to bribery and corruption within the government, especially regarding giving loans to people they only knew and giving out loans when it is near general elections. They said that there was inequality in the way loans were given to individuals. The entrepreneurs also said that lending institutions were attaching very difficult conditions to loans and that the loan process itself was very long. This puts a strain on many businesses, especially manufacturers as many found it increasingly complicated to keep their equipment up-to-date due to lack of funds, something that compromises their competitiveness as a substantial part of the machinery dates from the 1970s and was much less productive than up-to-date equipment. The SMEs said they would like to see the loan process speeded up and loosening of some of the conditions and restrictions for loans, for example the requirement for a lot of identity evidence especially for people who do not have enough educational background. Some of them said they needed more training in business skills especially with regard to loan requirements so that they were fully aware of what was expected of them. In general, most entrepreneurs suggested that business growth would be enhanced if they were given help with issues surrounding financial capital.

#### **6.2.2.3.11 Regulatory environment**

The regulatory environment covers factors that affect the ease and risk of operating a business in a country, other than the normal production, sales and profit/loss aspects. One of the important functions of a government is to create an enabling environment, which encompasses political stability, stable macroeconomic atmosphere, supportive infrastructure, competitive incentives and security. Regulations are an important aspect of the business environment, since they represent



the most direct expression of government's attitude towards businesses. One of the SAP policies was to stabilise the economies of most SSA countries and this policy impacted on the SME sector in the ways discussed in this section.

Although most of the entrepreneurs indicated that the government was unrestrictive towards SMEs, some entrepreneurs felt that the regulatory framework for industrial activity in Malawi was still restrictive in some ways, particularly with regard to the issue of taxation. They pointed out that, in addition to lack of transparency, the framework was characterised among other things by poorly adapted regulations and excessive taxation. In an unequivocal manner, irrespective of the size of the enterprise or the sector of activity in which it operates, the level of taxation, high inflation rates, bribery and corruption were mentioned as the main difficulties posed by the regulatory context. Bribery and corruption was in the top eight on the list of difficulties constraining business operations. For those entrepreneurs who went to buy goods from neighbouring countries, they said they had to bribe customs officials at the cross-border points instead of paying duty on imports as some of the charges were excessive and arbitrary: "one needs to set some money aside for bribing the customs officials so that you don't have to pay duty on the imports", commented one entrepreneur. Bribery and corruption in the government and government departments' officials confiscating their merchandise for no apparent reasons and with no explanation offered whatsoever, was also a major problem. "You have to give these officials a back-hander if you want to get your goods back", said one entrepreneur.

The majority of businesses did not need government permission to start their businesses. However, two-thirds of the individuals surveyed did indicate that there were government laws and regulations that they were required to comply with when running their business, but over half of the entrepreneurs also stated that they did not have to meet any kind of quality standards for their products, implying that the quality of these products could potentially be very substandard.

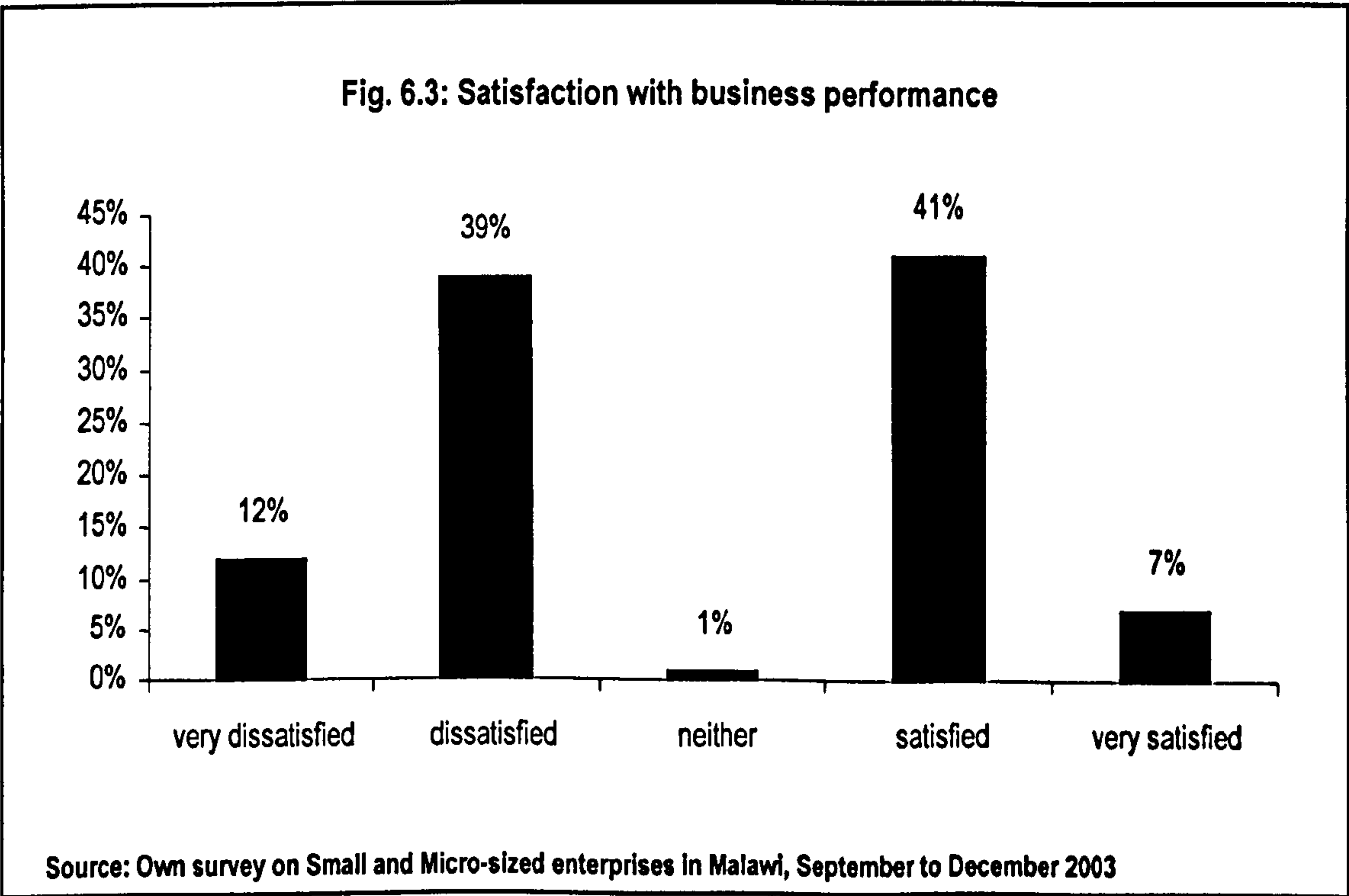
Consequently, although the Malawi authorities have undertaken to remodel and simplify the regulatory framework, these reforms are, in the opinion of several entrepreneurs, still insufficient. Many measures are still needed to establish a degree of confidence which can stimulate production. Entrepreneurs expressed that they would like to see other measures taken to make the current regulations more flexible or to reinforce them in certain cases. These included, among other things: increased access to public markets, simplification of procedures for loans and an end to bribery and corruption. They would also like the authorities to adopt measures which reinforce the



legislation on unfair competition and fraud. They also expressed that they would like the authorities to provide them with more protection as far as security was concerned in the country.

**6.2.2.4 General Entrepreneur Satisfaction**

The answers based on the satisfaction with the performance of their businesses varied very strongly, with approximately similar proportions satisfied and dissatisfied with the current rate of growth and the overall performance of their business. Thus, asked if the entrepreneurs were satisfied with business performance, 51% were not satisfied, 48% were satisfied and 1% was indifferent (Figure 6.3). Most reasons given for dissatisfaction included too many similar businesses around, too much competition, too much corruption, lack of capital for growth, high inflation rate causing fall in profits and customers who buy on credit not honouring the agreed credit terms.



Most entrepreneurs, however, indicated that running a business was difficult, largely because of competition, corruption and lack of capital for their business. The situation may have changed for some businesses since a large proportion of individuals whose businesses were operating before 1994 stated that their most difficult time was between 1981 and 1994. This suggests that the environment for small businesses may be improving. Unfortunately, many of these individuals were pessimistic about the future of their businesses, suggesting a lack of faith in current improvements.



### 6.2.2.5 Comparison of Survey results

Table 6.9 presents a comparison of findings from the entrepreneur survey with those of the Malawi GEMINI survey, which were discussed in Chapter Five. As well as some similarities of results, there are some differences between the two surveys. First, the GEMINI survey enumerated over 700,000 micro and small enterprises whereas this study was carried out on a very small number of enterprises. Second the GEMINI survey was conducted 3 years before the present study. The macro-economic environment as well as the SME policy strategy may have changed in the interval between the two studies. Third, the two surveys had different aims: the GEMINI survey gathered baseline data whereas this study went further and explored how SAPs and globalisation had impacted upon the SMEs. As there is very little comparability between the two surveys, comparison of the results, included in Table 6.9, has been made on only those few questions that were similar. Variables which were different between the two surveys were excluded from this analysis.

Table 6.9 Comparison of Survey results: Malawi GEMINI Survey with Own Entrepreneur Survey			
		GEMINI Survey 2000	Own Survey 2003
Size:	1-4 (micro)	91%	63%
	5-20 (small)	8%	33%
	21-50 (small)	1%	4%
Ownership:	Male	35%	58%
	Female	34%	30%
	Partnerships	31%	12%
Education levels:	None	16%	3%
	Primary education	69%	30%
	Secondary education	13%	44%
	Above Secondary	2%	25%
Having received Formal business training		10%	25%
Activity sector:	Commerce & Trade	45%	38%
	Services	7%	27%
	Manufacturing/production	48%	35%
Place of business operation:	Home	73%	36%
	Traditional market place	8%	11%
	Commercial district	2%	38%
	Roadside	10%	3%
	Mobile business	3%	9%
	Others	4%	3%
Main business constraints by ranking:	Input problems	1	2
	Market problems	2	5
	Financial problems	3	1
	Government/regulatory environment	9	3
	Transport problems	6	4
Data Source: Malawi GEMINI Survey 2000, Own Entrepreneur Survey 2003			



The data demonstrate similar pattern with regard to enterprise size in that there are much more micro than small-scale enterprises in Malawi. However in this survey, percentage of firms with 5-20 employees was much higher than in the GEMINI study and this could be for a number of reasons, one of them could be because of the different sampling methods used in the surveys. The GEMINI study used cluster and random sampling for the surveyed entrepreneurs whereas in this study it was a matter of interviewing whoever was available and willing at the time. On the other hand it could genuinely be that some of the firms in the 2000 GEMINI survey had grown in size by 2003. There has been, however, a decline in the proportion of female owned SMEs compared to the GEMINI study where it was almost equal. Again this could be because of the difference in the sampling methods. As for education levels, most of the entrepreneurs surveyed in the GEMINI study had only achieved primary education whereas in the 2003 survey there seem to be improvements as most entrepreneurs had either Secondary or University education. This could be because of rising levels of unemployment such that more and more educated people are resorting to starting a business of their own or it could be that the campaign for raising the education level of Malawians is bearing fruits. With regards to business training, this study showed a higher percentage of individuals who received formal business training than the GEMINI study although the numbers were still small, indicating that not many of the entrepreneurs have the necessary business skills, and much more needs to be done in this area.

This survey's results also show a different picture for the three broad sectors of activity. There are more service entrepreneurs and less manufacturing or production in this survey than the GEMINI study could find. This is probably more representative of the current trend where more and more entrepreneurs are engaging in service activities such as opening private clinics, private schools, telephone and communication bureaus, private transport service, and so on. The decrease in manufacturing could be the result of heightened import competition stemming from liberalisation of trade policy under the SAP. There has also been a shift in business operating locations. This study showed a lower percentage in those businesses operating from home than the GEMINI survey, and shows a slight increase in those conducting their business in a traditional market place. However there is a remarkable difference in businesses operating from commercial or industrial business premises. While there might be several explanations for this shift, one possibility could be that as more and more entrepreneurs are engaging in service activities, it is becoming necessary for them to seek business premises in an industrial or commercial district, therefore the increase may just be a reflection of that trend.



Both surveys asked entrepreneurs about what factors were hampering development of their businesses. In general, the same broad categories of complaints were cited in both surveys: those relating to finance; input problems; regulatory environment; and transport problems. However, in this study, finance problems ranked first followed by inputs problems whereas in the GEMINI survey inputs problem was first followed by market size problems and then financial constraints. One explanation could be that the macro-economic environment is getting worse in Malawi and this was also reflected in that government regulatory environment ranked third in this study.

It is hard to draw definitive conclusions from comparisons of the two studies due to differences in methodology. Despite differences in sample size or sampling method, both studies have highlighted similar constraints experienced by the SME sector in Malawi.

### **6.3 Summary**

Overall there was a general consensus on most of the issues faced by the SME sector in Malawi, by both the interviewed government officers and the surveyed entrepreneurs. To begin with, they all agreed that the country was not well equipped to compete globally and that new technology is required. There is generally a lack of skills and knowledge to recognise the opportunities and benefits of globalisation. The survey findings showed that profitability decreased among SMEs and many found it increasingly difficult to keep their equipment up to date due to lack of funds, something that compromised their competitiveness as a substantial part of the machinery dated from the pre-SAP period and was much less productive than up-to-date equipment. Another major issue inhibiting SME growth and development in Malawi was lack of finance for working capital and even the government strategy paper admitted that there was lack of capital support for SMEs. High interest rate was a major problem for business borrowers such that credit financed investment was not an attractive option as real interest rates were consistently in two-digit range. Many entrepreneurs also cited 'corruption' as another problem for when it came to applying for a loan from banks and other credit institutions. "If you don't have the appropriate collateral, you either have to know somebody in high places or you have to bribe someone in those institutions", these were the exact words of one of the surveyed entrepreneurs. It was particularly interesting to note that the entrepreneurs cited corruption within the government departments as one of the problems inhibiting their growth and the surveyed government officers also cited corruption as one of the major obstacles to private businesses. This confirms that there is a serious problem of corruption in the country, which affects the development of the SME sector, and whether the corruption has been enhanced by the opportunities brought by the SAP or otherwise, is a matter for debate.



There were also concerns, on both sides, over lack of competitive environment due to high transport costs, high inflation rate and poor trading arrangements and these were cited by the interviewed officers as some of the reasons why manufacturing sector was failing. They also all agreed that chronically high inflation was discouraging the formulation of long-term strategies resulting in increased uncertainty and transaction costs. There also appears to be not much inter-firm network or cooperation amongst SMEs themselves due to lack of trust. The survey results revealed that there were limited linkages between SMEs and large-scale enterprises in the country, and general lack of cooperation among the SMEs themselves. There was a non-cooperative business culture and this was also agreed by both the interviewed officers and surveyed entrepreneurs. However, for some enterprises, like those in transport, they were cooperating informally with each other and business associations play a very active role as there is at least some information being passed around and informal information exchange taking place.

Problems with the tax system are still important barriers to further SME development and the survey evidence suggested that there were a number of acute problems, faced by SMEs, connected with tax law such as the number of taxes and the amount of consolidated tax payments. Amongst the different types of taxes, the most 'unpleasant' ones for the sampled enterprises were surtax, market fees and municipal tax. Most of the entrepreneurs felt that these taxes were relatively high compared to the amount of profits they made, probably one of the main reasons why most of them would not formally register their businesses.

The survey also revealed that SMEs did not experience serious competition from large enterprises except in some specific product sectors, mainly building and construction materials and the most important source of competition was other SMEs. More than half of the surveyed SMEs reported this and typical sectors were food products, metal products, woven products and services. On the whole they all agreed that trade liberalisation had resulted in a flood of competing imports, which reduced the market share of domestic SME production. The government's concerns over an open economy was that domestic demand was being satisfied through imports leading to serious balance of payments deficit which could consequently lead to more borrowing and debt. The officials acknowledged that the government desperately needed to revive the manufacturing sector. Generally there had been very few changes in the businesses of the surveyed individuals, and the market had not opened up to them for foreign trade. Since most of the small businesses did not import raw materials from other countries or export finished goods to other countries, the changes that they had been involved with had been very small, other than the fact that there was an



increase in competition that they faced, and many of them were not well-equipped to do so. The findings confirm the fears and debates, which were presented in preceding chapters, that the SAPs, in particular trade liberalisation, has exposed domestic firms to competition from imports before they are able to increase efficiency and competitiveness and also that the manufacturing base has been rendered weak and inefficient, certainly for Malawi. It seems that, production of goods (such as chicken rearing, furniture making) for domestic market still remains much more important than exporting. The lifting of trade restriction would seem like a good thing for businesses, but for most of these small business owners it made no difference due to the fact that they did not sell their goods abroad anyway except for the influx of imports in the country.

In summary The main problems hindering the SME sector which kept cropping up from both phases of the survey were lack of capital for business growth, obsolete equipment, bribery and corruption, poor infrastructure, high inflation and interest rates, unstable currency value and competition from imported products. Referring to Figure 1.1 presented in Chapter One, the only indicator regarding positive impact of SAP, would probably be job creation in so much that the SMEs have provided employment for many people who would have otherwise been without a job. Even though most of the SMEs are just a means for survival for most people, one cannot imagine what the situation (bad enough as it currently is) and living standards of those individuals would have been like had they not been given the opportunity to trade freely. It should be borne in mind that the SAPs and political reforms in Malawi cannot be separated when analysing the situation, as it could be argued that due to political reform people were given freedom to engage in any entrepreneurial activities of their choice but on the other hand the free trade policy also played a major part in allowing cross-border trade, thus allowing individuals to go out to other countries to purchase goods for sale in Malawi. However, strong indications from the survey results are that there is increased competition, shrinking market share for local producers due to increase in imports, poor financial support system and poor infrastructure, all of which are indicators for negative impact of SAP. Since there are much more negative than positive effects, it can be concluded that in the case for Malawi, this sub-Saharan country is, without a doubt, being marginalised rather than integrated into the global economy and for many SSA countries, disadvantages of globalisation outweigh the benefits by far.



## Chapter Seven

### Analysis and Discussions

#### 7.1 Introduction

This chapter builds upon all the issues which have been considered in the preceding chapters, thus from findings from the literature to the findings from the empirical investigation within the context of globalisation and SAPs. It compares the theory of how the SAP was intended to integrate SSA countries into the global economy with evidence gathered from SMEs in Malawi, a SSA country, to see if SAP's objectives are being fulfilled. In Chapter Six, results of the empirical investigation, on how the SME sector has been affected by the SAP measures, were presented and further discussion of the findings is presented in this chapter.

The analysis of the response of the industrial sector to the structural adjustment measures is complex because it is subject to several, often-conflicting forces, the relative importance of which depends on the measures taken. The short and medium-term effects of structural adjustment on SMEs are by no means clear and there are many contrasting views (Stewart et al. 1990). The varying debates surrounding the SAPs have been shown from the wide body of literature, discussed in Chapter Two and findings from the empirical investigation. Hopefully, the country case study findings have shed more light on how SMEs have been affected by SAPs in Malawi. Discussions of the findings are presented in the following sections. The findings have been discussed within the context of the conceptual and theoretical framework set out in Chapters One and Two. Policy implications are also discussed in the final sections of this chapter.

#### 7.2 Discussions

For the purpose of measuring the impact of SAPs on SMEs, the discussions have been presented under four main reform components: (1) *trade liberalisation* including external sector reforms (2) *domestic deregulation* including elimination of price controls; reduction of restrictive wage and labour regulations; public sector restructuring including reduction of public sector employment; privatisation of parastatals and demand management including demand control and reorientation from domestic demand to exports (3) *fiscal and monetary reforms* including depreciation of the domestic currency, liberalisation of foreign exchange control as well as allocation; and (4) *supporting sectoral initiatives*. The impact of globalisation has also been discussed in a separate section. These are the same components described and presented in the Conceptual Framework in Figure 1.1 as they form the basis for analysing the impact of SAP and globalisation in this study.



### **7.2.1 Trade liberalisation**

Before the Structure Adjustment Programme was initiated, SSA's export and growth performance was believed to have been hobbled by restrictiveness of its trade regimes. It was believed that if these countries gave priority to liberalising trade and adopting structural reforms, they would achieve high growth rates (IMF 1999a). Basing on the findings from this study, Malawi has not greatly improved its export performance as expected. The picture that emerges for Malawi is that it has become a "buying and selling" nation rather than a producing one as a result of trade liberalisation. Trade liberalisation has led to sharp increase in imports but exports have failed to keep pace. Export performance has been poor on the whole and the problem is that a country can control how fast to liberalise its imports but cannot determine by itself how fast its exports grow. As said, Malawi relies mainly on primary products for exporting and it could be argued that this is not enough for economic growth of the country. Markets for primary products grow too slowly to fuel growth as prices received from these commodities have been declining, earnings are too unstable and linkages do not work very well. Manufacturing on the other hand provides a larger menu of possibility for efficient import substitution and increasing exports than is possible with primary industries alone. However, it could be argued that modern industry is knowledge intensive. It may result in jobs for the highly educated, but it is unlikely that jobs will be generated for the poor, especially the surplus agricultural force of rural Malawi, even when the growth rate of investment is increased in the private sector. However, Malawi's dependence on primary exports is not, in itself, the major problem. Terms of trade for Africa's exports have been deteriorating over the past two decades (IMF 1999a). In order to improve export performance, Malawi would need to address the numerous problems, such as infrastructure and scarcity of capital. As well as domestic policies, export performance will also be determined by enhanced access to industrial country markets. But despite their generally open trade regimes, industrial countries tend to have restrictions on imports of agricultural products, where much of Africa's export potential is concentrated.

As discussed in previous chapters, in Malawi the manufacturing sector is mainly tea, sugar and tobacco processing (primary exports). As discussed in Chapter Five, the primary sector accounts for over 40% of employment, 38% of which is agricultural (Table 5.1) and also that the most profitable sectors were those that relied on naturally occurring resources such as crops, forestry and construction, which could be argued that this is where Malawi's comparative advantage lies. Comparative advantage dictates an important role for primary exports, at least in the early stages of development. However, the relative factor endowments that dictate the export of primary products change with population growth, degradation of natural resources, capital accumulation, education



of the labour force and adaptation of newer technologies. An ideal situation would be for Malawi's comparative advantages to move, with development, away from land and resource intensive products towards manufacturers. Virtually all governments would like to see this gradual shift to a more industrial economy. It seems inconceivable that SSA can enter a path of sustainable development without considerable emphasis on manufacturing and building a strong export-base of manufactured products. Under structural adjustment, manufacturing in Malawi has been floundering. The manufacturing sector itself is not considered dynamic in the sense that its value-added is low and it needs to be diversified towards higher value-added manufactured goods in order to improve Malawi's comparative advantage. In general, the trade liberalisation policy has not yet made a positive impact on the integration process of the Malawi economy. It is not yet clear whether this is due to slow implementation of the adjustment policies, the long time lag required before such policies can transform the economy, or rigid production structures incapable of competing in the global market. However, not all problems faced by the sector are attributed to trade liberalisation. As noted from the survey respondents, lack of capital and poor infrastructure (roads, communication and electricity) are also major hindrances to the development of manufacturing.

It is apparent that trade liberalisation has impacted negatively on the manufacturing SMEs in Malawi in that they are not able to compete internationally and most of them are closing down. One way for increasing competitiveness would be for the SMEs to use the advantages that inter-firm networks can offer, thus to increase the use of external suppliers of inputs and specialities and concentrate on core competences. The entry of educated individuals into businesses has positive connotations given their education and skills levels, and to what extent these individuals move into manufacturing industry rather than trade and services it is not clear, but trade liberalisation has provided the potential for a new type of SME. On the other hand trade liberalisation has failed to shift resources in favour of the export producing sector away from producing for domestic market as it was intended to. It seems trade liberalisation was implemented, in Malawi, without identification of which SME products have potential to achieve export competitiveness, one of the failures of the SAPs.

Following the liberalisation of trade in agricultural products, the private sector has been expanding into retailing in agricultural products, an area that used to be an exclusive preserve of ADMARC, the public distribution and marketing agency. In spite of the efforts and recognition of the potential role that the SME sector can play in Malawi's economy and especially in the livelihoods of the



relatively poor, the sector remains small compared to other countries in the region. The country still lacks a national strategy and policy that can push the sector significantly forward, but the intention is there.

Respondents in this study, in particular the government officials, said that trade liberalisation has certainly not helped industrial growth. Many large-scale enterprises have closed down due to competition from imports. Competing imports are on the whole harmful to all domestic enterprises, but their impact on SMEs seems to have been restricted to particular sectors such as clothing/tailoring, as revealed by this survey. The Malawi study clearly confirms the views from the literature that competing imports are a bigger threat to larger enterprises, which originally were set up to substitute imports. The restructuring of parastatals and the elimination of state monopolies has to some extent opened up new opportunities for SMEs and there certainly has been an increase in the number of SMEs since most people became aware of the free trade policy. The high influx of new enterprises has also had a harmful effect, causing intense competition among SMEs and domestic market saturation. The number of SMEs keeps growing although the GEMINI study revealed that over 90% of them close within five years. However, in the absence of specific information on disappearance of enterprises, it is difficult to ascertain net growth attributable to pre- or post-SAP periods. There is however greater availability of imports in Malawi and their use has increased. In so far as small enterprises rely on inputs imported by other firms, the improved availability of imports comes with considerable price hikes. As a results, the credit needs of SMEs rise. The trade liberalisation process should have been accompanied by (or preceded by) other factors such as strengthening of local enterprises and farms, human resource technology development, as well as the build-up of export capacity and markets.

For Malawi, it appears that despite opening up, much less private capital flows to the country has occurred hence the country has missed out on the benefits that often accompany such flows: transfer of technology, management and organisational skills. The opening of the economy to foreign capital has not succeeded in attracting a significant flow of capital or technology into the country, especially into the productive sector and exports have not picked up either. Imports have grown rapidly, and present indications are of huge trade deficit. Foreign debt has increased significantly and servicing of the debt and repayment obligations are exerting pressure on the international BoP. The result of this has been a widening of trade deficits, deterioration in the BoP and continuation or worsening of trade external debts, which is ironic considering that SAPs initial aim was to correct the worsening BoP position of these countries. There seems to be an internal-



external conflict between the instruments and objectives of the reforms. For example pushing up interest rates to rectify BoP problems may on the other hand affect domestic investment in a negative way, as in the case for Malawi. Merely advocating free markets and trade does not necessarily lead to economic growth because the economy is much more complex than that.

### **7.2.2 Domestic deregulation and public sector restructuring**

The shift from government controlled to a more market-based policy regime is meant to create a business environment that enables entrepreneurs to respond quickly to emerging market opportunities and improve efficiency and productivity. The World Bank and IMF hoped that privatisation and market reform would somehow stimulate a group of entrepreneurs just waiting for the opportunity to respond with investment and production. There seem to be no productivity gains and certainly no positive growth performance of the Malawi economy. It seems the situation was misread, as most entrepreneurs in Malawi are involved in informal activities in order to survive and rely on formal jobs just to keep sufficient working capital to continue their informal activities. Many have been forced into informal activities out of destitution from economic crisis whose indication has been an expansion of such "survival" activities as hawking goods or making and selling small-scale food items. The income earned from these activities has been used to maintain declining consumption levels rather than to increase savings for capital accumulation and expansion. The domestic deregulation policy may have benefited the consumers since prices are very competitive and they are spoilt for choice with so many different types of imported goods. At the same time it could also be argued that living standards have gone down due to declining purchasing power of the currency, high inflation rate and decline in real wages. The deregulation can only be good for consumers if domestic economic expansion is somehow sustained sufficiently to ensure that there is more purchasing power in the hands of the consumers, which has not been the case for Malawi.

The impact observed was that private sector monopolies are the chief beneficiary, leaving little room for entry or development of new indigenous SMEs. Most opportunities tended to have been generated in trade, transport and services while far fewer took up manufacturing. On balance the result may be a net loss in industrial capacity. The elimination of domestic price controls has resulted in considerable price hikes which undo the intended effect of currency devaluation, thus raising prices of imports relative to domestic prices, and also raising the prices of material inputs and transport costs within the country. Stimulation of domestic incomes, which is a key to SME growth, is not happening at all and the curtailment of public sector employment has had supply side effect. Redundant civil servants as well as aspiring young potential entrants exit the public sector labour market and establish their own small enterprise. The government introduced measures to



reduce public spending to stimulate agriculture through improving the terms of trade, especially for export crops, like tobacco, and to stimulate investment and manufacturing export. The impacts of these measures on SMEs were difficult to trace and no doubt varied by sector and type of enterprise.

### **7.2.3 Fiscal and Monetary reforms**

As noted before, these reforms included curtailment of government spending, liberalisation of interest rates, foreign exchange, and the banking sector. Financial liberalisation measures seem to have had negative effects on the SME sector in Malawi. The effect has been a demand contraction for SMEs caused by diminishing purchasing power of their customers. Inflation has certainly not been curbed and high interest rates are a major deterrent to those involved in small businesses. There seems to be every indication that signifies the failure of the policy objectives of treating small manufacturing enterprises as priority when no appropriate criteria has been developed for assessing the credit-worthiness of applications from such enterprises. In the absence of suitable collaterals, banks have no other means of striving to attain a policy goal. Lowering of entry barriers into banking has led to a substantial increase in the number of banks operating in the country, mostly urban-based, although they are of not much use to the SME sector as over 70% of the SMEs in the country are rural based (GEMINI study).

Before the structural adjustment, the financial system in Malawi was very narrow. It essentially comprised the Reserve Bank of Malawi (central bank) and two other major state-owned commercial banks. Financial liberalisation allowed opening up of the market to new, local and foreign banks, and deregulating interest rates and foreign exchange control. It is, however, apparent that the banking services are still biased, available to only a few areas, and accessible mainly by the large trade and commercial entities. Small and micro-enterprises, both rural and urban-based, still face access difficulties.

One of the SAP policies was the external sector reform, which comprised of various measures to enhance the availability of foreign exchange and liberalise its allocation. The introduction of private foreign exchange bureaus has provided a major source of foreign exchange to the private sector without controls. Foreign exchange is now available with no restrictions. However, it appears from the study that most SMEs in Malawi do not seek foreign exchange and in as far as they have been relying on parallel foreign exchange and illegal imports, these reforms have had no direct impact in terms of prices. However, most entrepreneurs were finding it hard to understand or cope with the frequent currency devaluations coupled with high inflation rate. In all, the high levels of inflation



have had the unintended effect of seriously eroding the capital base of many SMEs in Malawi which, in view of the difficulties of access to credit, has diminished their capacity to adjust to changing market conditions. This study could not ascertain to what extent demand switching away from larger enterprises and in favour of lower-priced (and lower quality) SME products has taken place as a result of declining purchasing power in the domestic market. This could probably be one of the areas for future research work.

#### **7.2.4 Supporting sectoral initiatives**

The Malawi government recognises the important role of small and micro scale enterprises in the economic development of the country. Efforts that the government made towards development of this sector include creation and support of public and semi-public SME support institutions and encouragement and facilitation of the establishment of NGOs dealing directly or indirectly with SMEs. Malawi formulated a policy document for the development of micro, small and medium enterprises in 2001. The objective of the policy was to create an enabling environment for the growth and development of small enterprises and to maximise their potential to contribute to the country's economic development. The policy was formulated to address credit, raw materials, markets, entrepreneurship and management skills, infrastructure, technology and production costs. The government also formulated a national strategy for SME development, which forms a framework within which different policies and programmes are implemented to ensure the delivery of the most needed services to the SMEs in a cost-effective way. The strategy visualises a situation where large enterprises and parastatals will attempt to integrate SMEs into their production and marketing structures in such a way that would be beneficial to all segments of the economy. However, despite all these efforts the SME sector remains underdeveloped, as the macro-economic policy environment is still quite unfavourable for them. Business support has not been tailored towards the needs of specific areas, industries or certain small business size, and there is a poor level of assistance for micro and home-based businesses. Whatever the government and NGOs have done over the past years (as part of SAP or not) to assist SMEs with credit barely constitutes a trickle, as the majority of SMEs in Malawi were set up with own resources. A similar conclusion may be drawn with regard to training, which is predominantly non-formal.

From the discussions held with the government officers, there seems to be many donor initiatives intended to support SMEs in the country. However, many entrepreneurs expressed the view that there was not much support in terms of finance and training given to them. Twenty years on many have inadequate managerial and entrepreneurial skills and not much appropriate training is



available to them. Communication in terms of transport is still very poor and other infrastructural support system is equally poor. SMEs have not moved at all from low productivity informal sector to higher productivity formal sector. The majority of the SMEs are informal and they have been started up mainly as a means for survival, thus there is an expansion (multiplication) of SMEs rather than a deepening effect. Implementation of the SAP measures without the necessary support system seems to have failed the SME sector in Malawi.

As noted from the survey results, linkages with large firms and with other SMEs are weak in Malawi. One of the government's main goals for the development of the SME sector in the medium and long-term is to strengthen backwards and forward linkages and inter-firm cooperation within the manufacturing sector and between the rest of the economy. Industrial clusters and networks can provide economies of scale and scope to allow enterprises to lower fixed costs in exporting. On the other hand, inter-firm cooperation involves emotional stress in fairly small communities where everyone knows each other, and many are related and have a long history of intra-family feuds. Consequently it can be difficult to interact in a 'businesslike' manner. Moreover, cooperation, in particular in terms of deliveries and sub-contracting, will necessarily involve conflicts from time to time, and endless haggling between firms on price is not unusual. All this hampers the development of the sector.

Although the business regulatory environment has become unrestrictive, it is still not easy to access finance and the cost of finance itself is very inhibitive, causing a supply side constraint. As the financial problems cannot categorically be attributed to the formal financial sector only, there is a need to analyse SME financial needs and then find the optimal way to satisfy them. A differentiated approach is needed as different types of SMEs, at different stages of their life cycle, have different financial and non-financial needs which cannot all be well serviced from one single source. For instance, at inception, start-up capital will usually be obtained from personal savings or loans provided by friends and family. This will cover initial outlay for fixed investment in things like tools and working capital. Only modern SMEs can aspire to external funding for their start-up, which is limited in Africa and does not hold much promise even in the near future. Access to formal finance for start-up is poor because of the high risk of default among SMEs and due to inadequate financial facilities.

At the beginning, overall capital needs of SMEs would seem quite modest and the majority of the initial investment is used for fixed assets rather than working capital. Working capital is the lifeblood



of any business and balancing this seems to pose a challenge for entrepreneurs. If there is too little of working capital, the firm cannot function and there is a complementary need for it, which particularly tends to be underestimated at birth. Once a firm begins to produce, demand for working capital increases. In the survey, like most other enterprise surveys, entrepreneurs cited 'lack of operating funds' along with 'bad debts of customers' and 'not able to access a loan for working capital', as their most prevailing constraints. The principle use of working capital for SMEs is to finance labour, raw materials and other purchased inputs that go into goods produced for sale.

There are other means such as the informal sector which can satisfy the initial high demand for short-term working capital required by the SMEs. One way being credit from customers either through raw materials or cash down-payment to purchase raw materials (Kilby et al. 1984), and of course this is directly related to reputation of the producer. As quality and delivery performance become better known to consumers over time, customer prepayments should increase. Certain sub-sectors (like tailoring, furniture-making) could produce to customer order or even ask customers to provide the raw materials. This would keep marketing and production periods relatively short, inventory to sales ratio small, and corresponding demand for working capital relatively low. Terms of payments for receivables could be shortened and this will help to keep cash in the business flowing and enable them to respond to daily operating needs. For activities that may put a strain on the working capital, banks can provide long-term financing for increased inventory or other fixed assets, or market development initiatives.

Another way of sourcing working capital would be through the sub-contracting mechanism whereby, say, a larger firm supplies with the raw materials required to produce an order, for example fabricated metals. Another source of working capital is through accounts payable to suppliers of inputs. This grows in importance as an enterprise evolves and improves reputation. Since the perceived risks of longer-term lending to SMEs are deemed relatively high, not much term finance is provided by the informal sector (World Bank 1989d). Some fixed capital, however, can also be supplied by the informal credit market. Sources of fixed capital such as supplier credit and subcontracting become available when the SME becomes well-established and develops a good payment record.

There are however, limitations with these informal financial arrangements. For instance, they cannot provide the large sums of money for the long periods required for firms to grow (World Bank 1989d). Lack of integration of these informal sources, which are generally independent from one



another is also not conducive to building up reputation and generating information for formal lenders on the SME's evolving financial management ability. This is where government support or policy may come in to help integrate the existing informal financial institutions and help them with legal protection from embezzlements and mismanagement and creating an enabling environment for their operations. Financing is particularly lacking when an enterprise is being set up, when sales are still insufficient to improve the cash flow position. Unless access to a source of credit is available, enterprises find themselves in an extremely vulnerable position. This is the stage at which new financial mechanisms should be developed or the existing mechanisms made more flexible to allow for the support of viable investment projects. Finally at a later stage of evolution, SMEs may begin to have access to the formal financial market, thus after they have transformed themselves into modern enterprises and needing more capital for expansion. Capital for expansion or equipment replacement is one of the major areas in which formal institutions like banks operate. The banks tend to support operations, which are indicative of more mature enterprises, which have a better structure and have successfully got through the critical beginning phase. This usually benefits large and medium-sized industrial units, however.

In general, the reform measures have not worked very well to the benefit of SMEs in Malawi and no new areas of economic activities for them have opened up outside their local market niches. On the whole, since the introduction of the reforms, competition has increased in stagnating or marginally growing domestic markets and the main contributing source is the large influx of SMEs. At the time of carrying out this empirical work the SME policy framework on which the government and donor efforts were going to focus had just been formulated. It should be noted that the SME policy came into place 20 long years after the SAP was first introduced in Malawi.

### **7.2.5 Impact of Globalisation**

Globalisation has been seen to be very important to many businesses as at the heart of globalisation is the 'market' or at least ideologies of free trade and open markets and increased potential for flows of international market transactions. However, when discussed, globalisation is generally in the context of the larger businesses that are able to expand into foreign markets and do business across continents, either through the Internet, TNCs or other means. These businesses have money for marketing and transportation, and they adhere to extremely high standards of quality, for the most part. For these larger businesses, globalisation can maximize profits and make the importation of raw materials much easier and cheaper. Despite this, small businesses are suffering due to much of this global activity, and this largely comes from the fact that globalisation brings more competition for them without giving them any added benefits, as it



has been observed from the results of the SMEs in Malawi. While some SMEs in other parts of the world have demonstrated a capacity to compete successfully in markets, the majority of SMEs in Malawi have not moved to develop export markets or make best use of Information, Communication and Technology, while innovation and Research and Development remain poorly developed.

Many of these small businesses do not know about marketing and advertising their products, and they are unclear about standardisation. Standardisation has been talked about for some time and was generally returned to the forefront of the marketing challenge issue in the mid 1980s under the name of globalisation (Levitt 1983). Globalisation utilises a particular school of thought, which indicates that travel, media, technology, and education all have consumer tastes that are very similar and have differences that are only superficial and minor in scope. Those that believe in this strategy of adaptation seem to feel that globalising marketing would be the best way to move into the new technological advances that are taking place, but there are others that believe that the gap in differences for various consumers has actually been getting wider in recent years (Shaw 1999). Naturally, not all individuals that own small businesses wish to market to other countries, as was evidenced by the collected data, but there are some that do, and other small businesses may be forced to try to market elsewhere if they wish to survive the changes that are taking place in society.

Studies that have been conducted on this issue failed to address whether there were specific approaches to marketing and advertising products that are seen to be more effective (Jain 1989, Onkvisit and Shaw 1999, 2004, Shaw 1999). This idea of marketing is so foreign to the small business owners in Malawi that there is not much chance that they will figure out how to do it properly, or that they would choose to do it even if they could. However, the changes in trade restrictions have made things worse instead of better for many of these small businesses and they may have precious little choice when it comes to how they wish to do business in the future, and that is if they are serious and committed to developing their businesses further. Becoming educated about what they need to do next and finding the money to do it, however, are often serious problems. For those small businesses that do want to or decide to market their goods to other countries, there are many different ways that they can do this, and there are concerns regarding the level of effectiveness that their marketing might have. Unfortunately, the trouble that these individuals have in obtaining loans for their businesses forces many of them to not even consider the possibility of participating in a global economy.



For the SMEs in Malawi, localised advertising may be as far as they can go, but they can use some of the same techniques that global advertisers use in order to attempt to attract more customers. With little money, few government restrictions, and virtually no quality standards, however, moving out of the local market may be something that even the most ambitious and well-intentioned small business owners find that they cannot do. Many people in other countries are not interested in any product that does not meet some type of quality standard and therefore the idea of selling to any other country is not one that meets with much approval for many people. And as observed from the Malawi data, many of the surveyed entrepreneurs said that there is no formal requirement or guidance on minimum quality standards that they have to adhere to and that it is up to the individuals to decide whatever quality they want for their products.

Protectionism in the North is also to blame to some extent, not giving way to globalisation. Countries in the North do not only protect their markets, particularly their agricultural markets, they also heavily subsidise them. However, the governments of the North and IMF tell African countries to take away subsidies from their peasants who depend on them. Developing countries were forced via the SAPs to open their markets for foreign imports but most of the markets of the North still remain closed for imports of manufactured goods from the South. On the other hand it could be argued that even if the markets in the North were fully opened for the South, the goods themselves, particularly manufactured ones, would probably not be competitive enough in terms of quality standards and transportation costs as these other factors are also barriers in themselves. It seems, today, the macro-economy as well as the social policy is dominated by inhuman competition as the highest principle of the world market is economic efficiency. According to this principle industrialised countries are rewarded and developing countries rigorously punished. In Malawi, the productive sector is failing to develop the ability to withstand the intense competitive pressures that are associated with globalisation, although it can be argued that SMEs themselves do not really see imports as a problem. As revealed by the data in Chapter Six, less than 1% of the surveyed SMEs saw imports as a threat to their businesses, probably because most of them are involved in buying and selling rather than in manufacturing industries. However, for those manufacturing industries, be it micro or large, the lifting of trade restrictions, without proper institutional set-up and infrastructure beforehand, could be one of the most unfortunate things that have happened to business owners in this part of the world in quite some time, and there appears to be no end in sight at the moment.



The logic behind SAP as it affects industry was that import liberalisation, devaluation, reduction of protectionism and positive real interest rates will punish inefficient industries and reward efficient ones which are export-oriented, more labour-intensive and use more local raw materials leading to the country to exploit its comparative advantage. The result would be a prosperous and growing sector, which would greatly contribute to an increase in exports while using fewer imports. Unfortunately, for Malawi adjustment has not worked out as anticipated because management and labour skills are in very limited supply, finance is difficult to secure, information is costly, relations between firms are poorly developed, technology is difficult to obtain and costly to use, transaction costs are high and public goods are poorly developed. Opening up industries to the full force of international markets will hardly lead to desired results when institutions and capabilities are so weak.

### **7.3 Policy implications**

A number of policy implications can be drawn from the findings of the case study, Malawi. These arise out of, and are informed by, the conceptual insights afforded by this research. Contrary to much of the thinking which has underlain structural adjustment, the creation of an environment which is conducive to the development of the SME sector is not sufficient to ensure that optimal results are achieved. Indeed the response of the sector to the new opportunities, which arise as a result of the reforms, is conditional on a wide range of factors. These include the stage of development of the sector prior to the adoption of the reforms, the degree to which it has access to the resources such as skills, technology, credit and infrastructure, necessary to enable it to adapt to the new environment, and the level of political and institutional support accorded to it. Where conditions are not generally favourable, as in the Malawi case, SMEs are likely to be able to respond only in a limited and imperfect way to the economic opportunities opened up. In Malawi, for example, despite the immaturity of the SME sector and the poor institutional and policy environment in which it operates, SME activity has greatly increased in recent years. This activity has, however, tended to be concentrated in the trade and service branches such as petty trading and grain milling, with a much weaker response in strategically more important sectors such as manufacturing and capital goods. From the government's point of view, 'buying and selling' really does not create wealth, and as noted from interviews with government officers there were concerns expressed regarding the country undergoing de-industrialisation as a result of SAP. And if the country's long-term growth depends on the rapid growth of the manufacturing sector, then there is not much hope for positive economic growth in the near future unless there is some intervention to revive and encourage the manufacturing sector again.



The diversity of the different types of SMEs poses a problem from a development-strategy point of view. While it is true that all these types of activities are prevalent in the Malawi economy, from the perspective of articulating a development strategy for SMEs, it is essential to have a clear notion of which type of economic activities to promote actively and which to tolerate as an unhappy aspect of the underdeveloped state of the economy. Not all SMEs are deemed to have the potential to 'graduate' into viable enterprises. There is, therefore, a need to differentiate between different types of SMEs, in crude terms, 'survivalists' versus 'opportunistic' entrepreneurs, rather than perpetuating the current widespread practice of policymakers and planners in assuming the sector to be homogenous, with the problems and needs of all small enterprises seen as broadly similar. The opportunistic SMEs are motivated by pull factors such as achievement motivation, they take it as a challenge, they have a choice and are based on the perception of opportunity, recognise their own abilities and desire to increase wealth. In contrast, the survivalists are motivated by push factors. Thus, they are forced by circumstances whereby there are no other options available to them and are either faced with redundancy and a lack of employment opportunity. They are usually driven by the need to survive and are doing it for daily needs without re-investment as profit is used up on daily needs. They are also less privileged and skilled and are driven by external factors.

There are different policy implications for the different types of motivation and government may need to use different policy approaches to the different groups: sustainable economic development using the opportunistic SMEs as a development vehicle; and poverty eradication through a poverty relief programme. The government, with support from external institutions, may need to adopt policies which stimulate demand for opportunists, help them with development resources in terms of technology, encourage entrepreneurial team working amongst them and help them with establishing market linkages. There is the need for augmentation of production methods and technologies; optimising processes that exist and manage them; formation of support structures; expansion of product range and rationale; capability building for self-sustaining; training to effectively capitalise on indigenous knowledge systems for job creation and growth; indigenous knowledge should be conserved, valued and harnessed to develop products that relate to the culture and tradition of communities; and it needs to aid in turning the necessity entrepreneurs into becoming opportunity entrepreneurs, should they wish to do so.

To speak of one policy for the SME sector is incompatible with responding in a meaningful and flexible way to the totality of its needs. Quite often the urban-based large and medium-scale industry is seen as the motor of the economy whereas the informal sector, with SMEs of all kinds, is



seen as performing the dual function of providing cheap consumer goods to the poor and mopping up the underemployed. The empirical survey discussed in Chapter Five suggested that in certain sub-sectors, small-scale production were dynamic and these could play an important role in developing linkages with other sectors of the economy and in stimulating national economic growth. It is important that the institutional mechanisms established to assist the small enterprises recognise that certain segments of the sector have the potential to play a significant strategic economic function and merit, in consequence, integration into national economic planning.

SME access to modern technology, in terms of product manufacturing equipment, is extremely weak in Malawi. The process of technology acquisition has, for the most part been dictated not by a process of rational technology choice, but rather by buying whatever happened to come onto the market. In many cases, this has comprised old, broken machinery, which has been renovated or repaired by the entrepreneur. Poor state of equipment was cited as one of the major constraints on production by most of the government officials interviewed in Malawi. There is little hope that entrepreneurs will be able to plan their acquisitions in a more coherent way, as there is little information available to them on available technologies and sources of supply. In general, the weak response of the SME sector to the opportunities opened up by the SAP in Malawi must be understood in the context of failure of the institutions of the state to reorient themselves towards an improved provision of the services towards the sector.

The major issue which came out of this study, and which has persistently been cropping up in previous studies, was that SMEs' access to productive resources, such as credit was poor in Malawi. In this study (as in many others) it was revealed that access to credit was much the biggest constraint on increased production. In addition to that, a poor flow of market information together with liquidity shortages on the part of the traders appears to result in SMEs being starved of the required inputs. The formal banks have failed to develop means for the disbursement of credit, which are appropriate to the particular needs of SMEs. Securities demanded are generally well beyond the means of most SMEs, while a large amount of time is required for paperwork and administration of loans acts a further constraint. While the changing environment resulting from SAP reforms has been undercutting much of the long-standing protection of large and generally inefficient enterprises and stimulating increased output from smaller operators, the various support institutions, such as the banks, training institutes, development and information centres, have responded slowly, if at all, to the changing needs of the new economic actors. In many cases, this failure to respond has been a consequence of cutbacks in government funding resulting from the



SAP reforms themselves. Strong political and financial support would be necessary in order to persuade and permit these agencies to reorient their services to the needs of the SME sector.

The government may need to apply policies which would see that inflation was curbed and that the country's currency was stabilised, and this would give a lot of encouragement to entrepreneurs. In most developing countries devaluation is carried out for the purposes of closing large unsustainable excess of imports over exports, the most imports being luxury goods consumed by the urban elite. Currency devaluation can be a powerful tool for countries with severe BoP problems, a common phenomenon in developing countries. However, even if a country's currency weakens, its balance of trade will not necessarily improve as currencies of some other countries may have also weakened, allowing their local firms the same competitive advantage over home firms. Any policy that will increase foreign demand for the country's goods and services will improve the balance of trade position. This can occur when country's inflation is low or when currency value is reduced, thereby making the prices cheaper from a foreign perspective. However, there is a trade-off between some initiatives and other aspects of the SAP. For instance, the regime of restrictive monetary and interest rate policies targeted for macroeconomic stabilisation simultaneously increases the cost of finance for SMEs and constrains effective demand. Given that SMEs produce for the domestic market, stimulation of domestic incomes is the key to their growth. Unfortunately the effect of such measures as market-determined interest rate policies, restraint on growth on money supply and curtailment of government spending, result in the reduction of domestic demand and incomes which imposes a demand side constraint on the growth of SMEs. That is where intervention of some form may be needed. It has already been noted by the World Bank (1996a) that reforms through liberalisation, privatisation and stabilisation are not enough to create a vibrant economy. Building on such reforms requires major consolidating strategies to develop strong market supporting institutions, and to encourage the political economy environment in which they operate. This type of strategy intervention is supported by Huq and Tribe who said that governments need to determine how best they can work together cooperatively and complimentary with the private sector and NGOs in order to create a vibrant economy (Huq and Tribe 2004).

At the core of the argument for open markets is the proposition that markets create competition and competition stimulates the growth of productivity, which stems from neo-classical economics. As discussed in Chapter Two, both neoliberal and neo-classical theorists' strategies are based on market-led growth and do not pay much attention to non-market values, rules, relations and institutions. The neoliberal policies make universal assumptions about markets and the private sector, which is not the case (Stewart 1985). And they assume that land, labour, credit and product



markets exists naturally when in fact historically factor, product and financial markets are rare in Africa (Havnevik 1987). Family firms may operate differently from the neo-classical theory assumptions say of profit-maximisation within the sphere of production. They integrate production and consumption decisions differently, which leads to outcomes different from neo-classical assumptions (Lipton 1987).

The reform efforts need to be selective and focus on the binding constraints on economic growth and take into account of market failures rather than just follow the list approach of the Washington Consensus. Tribe has recently argued that: "many economists have failed to take account of the imperfect nature of markets in making recommendations relating to trade liberalisation..." (Tribe 2006:p54). He says that focus should be on the inherent asymmetries of economic power, within the international markets, which has increased to the disadvantage of many LDCs despite the promises of the benefits that the reform would bring to these countries. Competition and profit motive will force producers, farmers, industrial firms, service industries, to operate as efficiently as possible and to reduce costs whenever they can, translating into a more productive economy, so long as market failures are compensated. It is evident that the market alone has failed to produce the desired outcomes in Malawi and market-orientation is not the only factor contributing to growth: entrepreneurial talent, educated workers, infrastructure and a well-run government are also important.

In this study it has been shown that market forces are often led by, and hence favour, people and firms that are already successful. For instance, in Malawi banks are most likely to give loans to people who are wealthy and have money in their bank accounts. Thus, market-oriented growth may concentrate income initially, even while relieving poverty. This may justify a case for government intervention in international markets. As seen from the Malawi results, most government officers expressed desire to boosting the overall wealth of the country, thus to the benefit of all, both consumers and producers. Clearly, from the findings from Malawi, the manufacturing industries cannot compete with well-established industries in the developed countries. Before the SAP, most economists saw little benefit in government intervention and strongly advocated a free trade policy. However in order to allow manufacturing to get a toehold, the argument is that governments should temporarily support new industries (with tariffs, import quotas and subsidies) until they have grown strong enough to meet international competition. At the same time, the government has to be careful, with intervention in the form of subsidies, not to protect the inefficient rather than promote efficiency.



A final policy implication to arise from this study concerns the role of the SME sector in the economic development of the country. It is relevant to raise the question as to what the government can do, if anything, to restructure industry and what role SMEs can play within the SAP context. With regard to the role of SMEs, several policy choice questions emerge: to what extent should promotion of SMEs continue to be broad, covering both part-time and full-time enterprises, both rural and urban ones? Should one continue to focus on existing entrepreneurs or on entry of new and differently qualified entrepreneurs and enterprises? These are important policy choices. For example, a programme concentrating on enterprise development at universities among university graduates and technical training institutes and agricultural colleges may reach far fewer would-be entrepreneurs than large low-cost programmes of enterprise development in rural and urban areas, but which one would achieve better long-run results? Put it differently, should direct assistance programmes be 'widened' or 'deepened'? The former would lead to low-cost minimum package programmes of micro-enterprise formation and expansion, while the second would imply a selective concentration on much more expensive enterprise transformation programmes and associated development of techno-institutional support systems for particular product sectors and areas. No doubt the most desirable situation would be a combination of both. However, the optimal mix should be the result of a deliberate policy reflection and not the accidental outcome of an unplanned mix of NGOs or of donor agencies in the countries concerned.

#### **7.4 Summary**

The aim of this chapter was to further analyse and discuss the empirical investigation within the theoretical context set out in earlier chapters. It brought together and reviewed all the issues, regarding SAPs, Globalisation and SMEs in Malawi, raised throughout the study. Two theoretical concepts of Globalisation and SAPs were used. And working within this framework, fears and arguments regarding marginalisation of SSA, certainly for Malawi, have been confirmed. The SMEs in Malawi, like many others in SSA, have no capability to compete against imports or secure export markets. Trade liberalisation has condemned local industries to bankruptcy, hence a waste of existing resources. Malawi lacks the physical and social infrastructure to support SME growth and trade liberalisation has not improved the performance of the manufacturing sector. Those SMEs that have the potential to be competitive in the world markets are constrained by lack of finance, high cost of inputs, lack of appropriate training programmes and technical capacity. Malawi's economic growth and SME performance is also impeded by its landlocked status, dependence on a



single cash crop (tobacco) for the bulk of export earnings and poor incentives for foreign and domestic investment.

It has been argued that there is weak evidence in support of claims that macroeconomic policies, price distortions, financial policies and trade openness have predictable, robust and systematic effects on national growth rates, except possibly in extreme cases (Rodrik 2006). Even the WB admitted that only seeking efficiency gains does not amount to growth strategy (World Bank 2005d). As discussed in Chapter Two, emphasis is now on building and strengthening institutions. It has been argued that trade liberalisation does not work if fiscal institutions were not in place to make up for lost trade revenue, capital markets do not allocate finance to expanding sectors, custom officials are not competent and honest enough, and labour market institutions do not work properly to reduce transitional unemployment (Rodrik 2006).



## **Chapter Eight**

### **Conclusions, Reflections and Suggestions for Further Research Work**

#### **8.1 Introduction**

The main aim of this research was to analyse the impact of globalisation and structural adjustment on small and micro enterprises in Malawi. Objectives for achieving this aim were set out and a theoretical context within which these were to be achieved was discussed, together with the research methodology. Literature was reviewed on the study concepts of globalisation and SAPs and also the socio-economic background of Malawi was discussed prior to the empirical investigation on SMEs in the country. Survey findings were analysed and discussed, and this final chapter concludes on the whole study, makes suggestion on areas which the researcher feels would be interesting for future research work and presents some final personal reflections.

#### **8.2 Conclusions**

The first objective of this study was to analyse the impact of SAPs, in particular trade liberalisation, and consequences of globalisation on the small to micro size enterprise sector in Malawi. Findings from the first phase of the study indicated that SAP resulted in growth in numbers of SMEs particularly those engaged in trading activities. According to those interviewed, trade liberalisation has resulted in disinvestment in the manufacturing SMEs. SMEs in Malawi face both supply and demand constraints some of which are shared with large enterprises. On the supply side, major constraints include: lack of skills in export marketing, export procedures and related aspects; inadequacy or absence of credit facilities in general and export finance in particular; lack of appropriate technologies to produce goods of high quality; and very small size of individual SMEs which limits their capacity to meet large export orders on a regular basis. On the demand side, a major constraint is the lack of information on the export markets, including that of Southern Africa, and on the products that Malawi can supply. However, even if the SMEs were to manage to get export orders, there are other constraints which raise transaction costs like high transport costs right from within the country and en route to the export destinations, especially foreign markets outside the Southern Africa region. As a result it is not easy to offer internationally competitive export prices that at the same time ensure viability of the enterprises.

Contrary to the belief that SAP would permit a private sector that is more competitive, dynamic and efficient in allocation of resources, it seems to have brought about more problems than anticipated and even more of a cry for help from the small enterprise private sector in Malawi. All the surveyed



entrepreneurs, government and non-governmental officers agreed that SAP measures have to some extent impacted negatively on the SME sector and the economy as a whole. For all those factors (international market share access, productivity, competition, industrial growth) that were originally believed would facilitate integration into the global economy, the majority of the participants gave responses which were not very encouraging, and from which one is tempted to draw the conclusion that the country is being marginalised rather than globalised into the global economy. It appears that the SAP projections have been proved invalid in the case of Malawi and that those SMEs involved in production are not coping very well with the external competition as most of them indicated that they would not be able to compete on the international market due to lack of capital.

The second objective was to analyse the response of the SMEs to adjustment measures and if the enterprises were becoming more competitive and efficient as predicted, in terms of export growth and increase in share of domestic market. Reaction and response of individual entrepreneurs very much depends on their judgement of the situation. The responses can range from moving the company to changing the product, the service or the production process. Going into a new line of business altogether is also a possibility, and in volatile environments entrepreneurs often keep options open by developing several activities simultaneously, as was the case for some of the SMEs in Malawi. Most of the entrepreneurs in Malawi indicated that starting up the business was their response towards trade liberalisation, whereas a small number of them either invested in modern equipment diversified their product range and a very small proportion of them sought export markets. The majority of them commented that they did not want to miss out on new opportunities although those who already had businesses said they did not feel the benefits of free trade at all. In general, there are clear indications from the study results that export growth is not happening at a fast enough pace at present. As export growth is fundamental to economic growth, it can be concluded from the results that SAPs have failed the Malawi economy as a whole.

The enterprise survey proved the existence of a potential base of dynamic enterprises, the creation of which was stimulated by the economic liberalisation policies pursued since the beginning of the 1980s. In particular this is the case for micro and small enterprises in the food-products sub-sector, which operate in an environment in which competition has intensified because of the increase in the number of enterprises, which are trying to get around the growth constraints of the narrow local market. The micro-enterprises are better integrated in the local economy, where they try to exploit the resource base; they also seem to have responded best to the incentives offered. They are



blocked in their expansion, however, by constraints on supply (access to credit, procurement of raw materials), unlike the small and micro sized enterprises which have demand problems such as limited markets and competition from imports. The availability of collateral and other sources of guarantee represent a necessary precondition of access to credit markets. The inability of banks to evaluate different enterprises and monitor their behaviour is creating a real failure of credit markets. Since most informal SMEs have not established reputations with the banks and because of scarce information on their profitability, access to credit markets is impossible or very expensive. In addition, general lack of collateral, widespread use of informal, non-registered forms of financing and institutional inefficiencies makes banks reluctant to finance this kind of enterprises.

From the entrepreneur perspective the enterprises are not competitive enough and most of them are just a means for day- to- day survival, which is not good for sustained economic growth of the country. The general consensus among the interviewed NGO and government officers was that free trade at the moment is not conducive to economic growth due to the increase of 'buying and selling' activities of SMEs which in turn is resulting in large drainage of foreign exchange reserves out of the country, thus there is not enough production and exporting to create wealth for the nation. In addition to that, the government has not been able to control and obtain any tax revenue from these enterprises since the majority of them are informal hence there is not enough funds for the government to spend on infrastructure and public sector development for sustained economic growth.

The third objective of the study was to analyse the local production and distribution networks that exist and to see if free trade has created opportunities for making new and profitable connections. From the survey results, inter-firm linkages are practically non-existent between the SMEs and large enterprises in Malawi. Very few SMEs receive subcontracted work from large enterprises and not many of them supply the large enterprises either. It appears the most common transaction is when SMEs buy supplies and inputs from the larger enterprises. The larger enterprises do not seem to reciprocate by buying material or supplies from the SMEs, and this is a failure of the network system, which is supposed to connect the local SMEs to the global system. The SMEs are not connected at all to the global economy in terms of their output being bought by larger companies or them exporting to other countries. Overall, the SMEs are based in local markets, produce single consumption goods and have no formal training, thus their system characteristics are based on local needs and resources.



The fourth objective was to analyse the new environment of 'free trade', to see if it is conducive to SME development and growth. It has been shown in the Malawi case that, while a policy of 'free trade' is widely accepted and its benefits are theoretically attractive, in practice it may not always be an optimum policy as some form of intervention may be required. It has been shown that there are distortions to SAP policies, for instance, SMEs not being able to access resources and export markets, hence the need for policy reform, from both the national and international community, to correct such distortions and create a level-playing field, if that is possible. In previous eras, most developing economies' SMEs were operating in protected markets. But increases in globalising economy, with free trade, industrial niches have become highly competitive such that it is also essential that the SMEs themselves develop the capacity to learn, so that they can adjust to changing circumstances. Changes in world prices throw the BoP into deficit, excessive spending fuels inflation, and drought or other natural disasters disrupt production. Unless government counteracts these economic shocks, they create greater uncertainty and higher risks of private producers and investors, who take evasive actions to reduce further future investments and worsen the crisis.

In conclusion it can be said that, despite adoption of SAP measures, Malawi does not seem to have succeeded in integrating into the global economy. Two theoretical concepts were used in this study: Globalisation and SAPs. Working within this framework, fears and arguments regarding marginalisation of SSA, certainly for Malawi, have been confirmed. All trade and investment indicators suggested that (despite liberalising the economy and implementing most of the required policy changes) Malawi's economy was in the process of being marginalised rather than being integrated into the global economy. The World Bank and IMF prescribed the SAP with the intention of fostering economic growth and strengthening the Balance of Payments position. BoP was seen as being caused by price uncompetitiveness and excess demand. The 'cure', therefore, was to admixture devaluation, demand-contraction and a restoration of the price mechanisms for the allocation of scarce resources.

From the study findings, this has not worked out as intended for Malawi as the BoP position is still as worse as ever and the steep fall of the currency value is hurting business as this is raising the cost of production imports and price of exports. Much SAP took place without a great deal of thought as regards to its relevance or understanding of the underlying economic problems that the SSA countries face in the longer-term. Many of them, like Malawi, are internationally very weak, with an over-reliance on primary product exports in a highly unstable world market. Given that



opportunities for expanding exports to regional and international markets do currently exist, not much is being exported by the SMEs, and exporting tends to be a one-off activity due in part to supply constraints in producing large quantities and demand constraints resulting from protected markets in the developed economies. According to MEPC, Zambia, Tanzania, and South Africa offer Malawi better export opportunities than other countries. However, these opportunities can be exploited only when the various constraints, discussed in previous chapters, are overcome.

The study analysis also brought out a number of policy implications for the government, SMEs inter-firm relations, developed economies and international organisations. It involves the adoption of a strategy that runs against the advice given to the developing economies of non-intervention. Some form of policy intervention is required if the SMEs are to participate in the global economy and progress forward. Sound fiscal and monetary policies are essential for macroeconomic stability, which is a necessary condition for sustained economic growth. A dynamic market economy also depends on basic institutional foundations including secure property rights and effective system for enforcing contracts and an efficient regulatory environment that does not impose undue barriers on business activities.

A combination of Globalisation, SAPs and SMEs is such a broad area to be covered in one research hence there was a limit to what could be covered in this study, both for financial and timescale reasons. Also, Malawi, though a good country area as a case study on the subject, impact may not necessarily have been representative of other SSA SME experiences and how they have been affected by the SAPs and globalisation. Hence the need for further research work and suggested areas where this study failed to touch upon has been highlighted in the following section.

### **8.3 Further research work**

As well as answering some questions and highlighting some problems, this study has also raised some more questions, which require answers, and other issues have surfaced that may need to be studied further. The true impact of SAP may not be fully realised at present as trade liberalisation took effect in 1995 in Malawi and this study was started in 2001, thus six years after. Probably it would be best to give the sector more time, say up to around 2007, and carry out a repeat or follow-up study to see where, on the development, growth and economic integration line the current SMEs are going to be positioned. It is also important to note that there is a need to replicate this study by using more measures and a larger sample which covers SMEs operating in different geographical areas of the country as this study mainly concentrated in two administrative districts, one of which is not heavily commercialised.



The non-availability of finance has been the most frequently cited problem encountered by SMEs in Malawi and the inability to raise finance is attributed to limited access to bank funds. There seems to be all kinds of entrepreneur surveys that have been and are still being conducted but not many researchers have approached or conducted a survey to find out what the bankers' problems or issues are regarding lending to SMEs in Malawi. There is the need to conduct a study among bank managers (those who represent the domestic banking industry) regarding criteria for lending to SMEs, in order for both parties to understand each other. The first question is: are the banks able to understand their SME customers, in particular, when processing loan requests from them? Bankers may have a preconceived attitude that they perceive SME owners as potential non-performers, and thus become reluctant to provide them with bank loans. That attitude needs to be discarded, and replaced by one that, instead, focuses on understanding the needs of SMEs they serve or want to serve. It is hoped that the information found in such a survey would provide bankers with insights into the needs and wants of SME customers. There is also the need to compare perceptions of both bankers and SME owners in order to bridge the 'understanding gap' from both sides. This understanding should help bankers to develop appropriate strategies and attract more customers from the SME sector. The second question is: how can SSA SMEs overcome finance and credit constraints? One of the robust findings from the Malawi survey was that personal savings, and not bank loans, are the main source of start-up funding amongst the SMEs. As a result of this, informal credit schemes (borrowing from other individuals) predominate. This underlines the importance of research into informal credit schemes and entrepreneurial networks in the country.

There is a need for identification, analysis and evaluation of key competitiveness and growth factors of SMEs in Malawi. An extensive survey effort is required to identify those factors. Firstly to explore and identify problems, and then prepare the future staffs coming out of the educational system according to the needs observed in the enterprises. If the country is to produce future specialists with appropriate management skills there is a need to conduct such a survey and analysis, and the results would allow the formulation of recommendations for the curricular development and teaching methods improvement. There may also be a need for further work on assessing impact of the support initiatives on SME sector development, to see if they are making any difference at all and who exactly are they targeting and what strategies they are using and if they need changing if they are not working.



Further research is also needed on entrepreneurial networks and clusters. Networks and clusters provide information; assistance and examples; stimulate innovation; and transfer technology and skills (Brautigam 1998:3). The role of social network capital in overcoming the negative features limiting SME growth and survival, are important topics for future research in Malawi and other SSA entrepreneurship. There is a need for the analysis of the production networks and the transactions immediately necessary to maintain it, a need to understand what kind of networking takes place among sets of companies, both large and small defined by industrial sector and location and investigate what kind of supporting input, repair and marketing networks that are maintained in a particular area, thus who deals with whom, where and how.

As most of the interviewed government officers expressed concerns over the weakening of the manufacturing sector, there is a need for conducting detailed analysis of the manufacturing sector in Malawi. This should be a systematic investigation of possible determinants of success or growth of manufacturing SMEs, aimed at identifying those factors impacting on success or failure of manufacturing in Malawi. This type of study would provide some useful insights to both manufacturers and policy makers in the country. The surveyed government officers acknowledged that there is lack of knowledge on how the entrepreneurs can access export markets but not much seems to be done to help the SMEs in this regard, probably there is also a lack of knowledge, skills and resources amongst those officers interviewed. There seem to be a lot of activities at regional level regarding trade agreements with neighbouring countries but this study could not establish whether this information is relayed to SMEs. However, with other problems like transport and communication, border procedures and so on, it is not very attractive to SMEs to export even regionally. A study could be carried out to find out how much knowledge on export markets the government itself has, how this information is passed on to entrepreneurs and what is being done to encourage production for exporting.

The SMEs would eventually need to enter the production and exports of high-technology manufactured goods. One notes, with sympathy, constraints faced by those involved in manufacturing in Malawi, one of them being technological obsolescence, rendering the goods produced from this non-competitive. Indeed, one of the strong arguments for the trade liberalisation in SSA countries was that greater openness would allow their SMEs to more rapidly assimilate new technologies. However, the Malawi geography, lack of clusters and high transport costs limit the transfer of much needed technologies. Technology cannot be simply transferred to an SSA economy or SSA entrepreneur like a product. The reason is due to the difference between capacity and capability as most new technology involves tacit knowledge and a learning process. Further



more there may also be domestic policy influences that hinder the transfer of technology to entrepreneurs. Research should determine to what extent this applies to Malawi, and how a more conducive learning environment for technological innovation and adaptation can be established.

It was interesting to note that people responsible for policy (government) also cited electricity power cuts, poor infrastructure and lack of modern technology as some of the major contributors towards collapse of the manufacturing sector. This study could not establish exactly why the government is unable to tackle these issues. They mentioned currency devaluation, water supply, inefficient telecommunication services and high rate of crime, all of which could emanate from government cuts in public expenditure, which was one of the requirements of SAP. A study could be carried out to find out exactly, besides SAP, what is limiting the government from tackling these issues.

Africa remains the world's poorest continent, and it is worth asking whether entrepreneurship can make a difference to economic growth and development in SSA. Answering this question would require rigorous research into African entrepreneurship and the role of political freedom and reform. More research on Africa entrepreneurship, in particular its relation to economic growth and export performance would have to be carried out and disseminated. Exporting is seen as one possible strategy for economic growth open to SSA but the question is: can SMEs in Malawi export manufactured goods? There is a need for research on relationship between SMEs and international trade. Another particular vexing question concerns the extent to which the informal businesses in Malawi can be characterised as entrepreneurial. It is generally assumed that the informal sector business provides little real economic growth or dynamism. Such businesses are often assumed inefficient, and survival-oriented and whose proprietors would gladly take jobs in the formal sector were they available or had a choice. From the responses received with regards to motives for starting up a business, it appears that these individuals enter the entrepreneurial market place without the prerequisite motivation to be entrepreneurs. Meanwhile, the government targets entrepreneurship development policies at people who have become self-employed irrespective of whether or not they are entrepreneurial. It may therefore be questioned as to why fiscal resources should be channelled to this sector if there are no positive social returns. Work needs to be carried out to explore the extent to which the informal SME sector is entrepreneurial so that the government can take different approaches to the different initiative types.

More detailed information such as geographical limitations of the country could be incorporated in the analytical framework to see if the SAP effects are attenuated. Geographical factors may be



important to understand the difficulties faced by entrepreneurs in Malawi. Geographic features that hinder entrepreneurship include: a very high concentration of land in the tropics (backlog in productivity growth as tropical climate pose inherent difficulties in agriculture and public health); and a population heavily concentrated in the interior, for instance, Malawi being a landlocked country and thousand of miles away from the coasts and far from the closest core markets in Europe. These factors raise both domestic as well as international transport costs. It has been estimated that the cost of international transport for landlocked developing economies are on average 50% higher than for coastal economies (Radelet and Sachs 1998). It has also been argued that as far as geography is concerned, it is specially climate and the environment for food production that limits the development of entrepreneurship in these countries (Diamond 1998:398). Geographical factors could therefore be incorporated in further research work on SMEs in Malawi.

Finally, it would also be interesting to analyse impact of SAP, in particular trade liberalisation in Malawi, using data from large enterprises as well. There is lack of sufficient research on the role and impact of large enterprises. Better research on the dynamics of large enterprises may throw more light on the determinants of small enterprise size in Africa as well as local indigenous industrialisation and the functioning of networks and the success or failures of industrial clusters. It would be interesting to identify those enterprise characteristics, which have proved well suited to the economic environment created by the SAP process – as well as others that have been penalised by it. A comparison of Malawi firms with their counterparts in other developing or neighbouring countries would also be a fruitful future research avenue.

#### **8.4 Reflections and final remarks**

Carrying out this work has been an enjoyable experience as work touched upon those academic disciplines that I have enjoyed throughout my education life, from Primary school to University. When I was reading up all types of literature, it brought back memories of how much I used to enjoy geography classes at primary and secondary schools and how much pleasure and excitement I used to get from attending undergraduate lecturers in statistics and economics, and population studied at masters post-graduate level. All this shows that most of the academic disciplines are getting more and more interconnected and interlinked just like globalisation itself! Considering how the global social and economic environment is now, it makes more sense to research social issues from all points and angles of academic disciplines, and there is no doubt that my knowledge and skills developed through studying a wide range of subjects and disciplines contributed to the shaping of this research. At the same time it has been a long and hard journey and I was fortunate



enough to have the full support from all my supervisors and family. There have been times when I wanted to give up and asked myself several times what the point of all this was and who was going to listen to what I had to say or found out from the entrepreneurs. And I have always been comforted by the thought that: I am doing it for all those small entrepreneurs in Malawi who are struggling to make it in this globalising world and who need someone to speak out on their behalf and tell their story to the world and I hope that this research has achieved that. The supervisory team and I are currently working towards publishing articles from this study: one on the SME results and one on policies and some contextual material. *This should help disseminate the findings of this study to a wider community including international and national policy-makers and I hope that many influential individuals and organisation will read the articles and make some positive changes to policies which will help and benefit not only the Malawi SMEs but also other SMEs in the SSA region.*

The experience of carrying out in-depth interviews with the government and NGO officials has enabled me to appreciate the bureaucratic process of the civil service. For example trying to arrange an interview where there was no known contact was extremely difficult; or trying to obtain a document on a diskette or printed form required me to go out and buy paper and floppy disks myself, things which one takes for granted in England when requesting information of some type from most organisations. However, ethnic links with Malawi National Statistical Office (NSO) and colleagues I went to University with, who are now working for the government, made possible and easy to obtain official government publications and to arrange for interviews, especially at short notices, which would have taken longer if I did not have those contacts.

Having to carry out the work with no financial support at all has been the most difficult part of this project when one considers the costs of purchasing a computer to carry out some of the work at home, printing and photocopying costs, hiring a research assistant and buying stationery and other consumables. I initially assumed that I would be able to manage to carry out the entrepreneur interviews myself and that I was going to be able to take some time off work and get to Malawi, spend three weeks carrying out the field work only to realise that I had underestimated my financial situation as I had no funds to finance the trip and it was not possible to take three weeks off full-time employment. I can only speculate about the difference it would have made to my research if I had carried out the face-to-face entrepreneur interviews myself. Nonetheless I regret missing out on the experience of having to talk to the entrepreneurs myself and hear it first hand. But I take comfort in the thought that at the end of the day, their opinions were heard.



As well as raising a young family and holding full-time employment was very hard going but I can only say that it was worth the satisfaction of completing the project and knowing that I have made a contribution to knowledge and hopefully contributed, though not directly, to the improvement of lives of millions of entrepreneurs who are going to benefit in the long term through policy changes.

This study has illustrated the unequal nature of the functioning of the global economy. Obviously this brief survey has not been exhaustive, but it has illustrated the breadth of the case for international reform. The outcome of SAPs has essentially been a consequence of complex social processes and that is why up to today there is still a revolt against the pressures of globalisation, by those who are loosing out from the process. Inevitably the discussion on trade barriers by the developed economies and adjustment policies is still at the forefront of international political discourse. This brings us to the urgent need to articulate new visions of how the developing economies might be transformed, which have been highlighted in this study. It is hoped that this study will serve in some small way to open up the possibility for genuine policy alternatives to SAPs, and add to the millions of voices worldwide campaigning for 100% of debt cancellations of the developing economies and opening up developed markets to the SSA agricultural and other products. It is also hoped that the study will help policy makers gain a clear picture of the SME sector, as an input into the identification of possible strategic priorities for economic growth programme interventions.



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# Appendices

## Appendix 1: SAL Programme in Malawi

<b>I IMPROVEMENTS IN BALANCE OF PAYMENTS</b>		
<p><i>A Smallholder production</i> Slow output growth and export stagnation</p>		
<b>SAL I Policy measures (1981-84)</b>	<b>SAL II Policy measures (1984-86)</b>	<b>SAL III Policy measures (1986-87)</b>
Annual review of smallholder prices using Bank-approved methodology. Increase in 1981-82 cotton producer price. Review of livestock sector prospects and incentives. Review of ADMARC's marketing and storage operations.	Continued use and improvement of the price setting mechanism. 80% reduction in the 1984-85 Fertiliser subsidy with complete removal by 1986-87.	Continued use of the price-setting mechanism, with Bank approval of 1986-87 prices. Fertiliser subsidy to be removed by 1989-90, with Bank approval for 1986-87 prices. Bank monitoring of the Fertiliser Project. Acceleration of ADMARC's rationalisation. Relieve ADMARC of certain financial burden of certain developmental activities. Expand the role of private traders in agricultural marketing.
<p><i>B Estate production</i> Excessive reliance on tobacco and tea exports. Rising input costs, shortage of management talent and land.</p>		
Study on tobacco market prospects and on tobacco estate diversification.	Revision of the proposed programmes for estate extension, management training and credit provision.	Set up a pilot estate credit scheme. Prepare management training and extension programmes.
<p><i>C Energy</i> Rapid rise in petroleum-import bill and depletion of domestic fuel wood supplies.</p>		
Energy sector survey on prospects, new investments and price policy. 1982-83 fuel wood price increase.	Preparation of Energy Action Programme and medium-term Energy Investment Programme.	No policy actions proposed.
<p><i>D Agro-industrial investments</i> Need to exploit investment opportunities to earn and save foreign exchange</p>		
Reform of Press Holdings and MDC to enable them to undertake new investments. Adoption of appropriate price incentives and wages and income policy.	Conditionality the same as under SAL I	Conditionality the same as under SAL I
<b>II PRICE AND NON-PRICE INCOME POLICIES</b>		
<p><i>A Wages, prices and institutions</i> Need for more frequent adjustments to maintain incentives and prevent distortions</p>		
Government review of price control system to improve flexibility. More frequent parastatal tariff increases in line with cost evaluation. Increase 1981 Blantyre Board tariffs. Prepare plan for implementing economic housing rentals.	Prepare price liberalisation programme and decontrol substantial number of items. Annual review of parastatal annual accounts and tariff increases where needed. Address issues of housing subsidies.	Complete price liberalisation programme by end of 1985. Review 1964 Industrial Development Act to encourage competition and restrict protectionist use of industrial licensing system. Ensure importance of goods that compete with domestically produced goods. Strengthen Export Promotion Council, prepare an export promotion policy, set up an Export Financing facility.
<p><i>B Exchange rate</i> Need for periodic review</p>		
Periodic review under IMF Standby.	Periodic Review under IMF Extended Fund Facility (EFF).	Government to continue an active exchange rate policy.
<b>III RESOURCE MANAGEMENT</b>		
<p><i>A Interest rates</i> Adjustments to keep real interest rates positive.</p>		
Periodic review under IMF Standby.		No policy actions proposed.
<p><i>B Public enterprises</i> Need to improve profitability and operational efficiency</p>		



Develop investment programme for Air Malawi and Malawi Railways. Review MDC's financial position including debt and equity needs. Review management budgeting of MDC and its subsidiaries and prepare long-term plans.

Implement findings of various studies on operational and financial improvements in individual parastatals. Strengthening and clarify the role of the Department of Statutory Bodies. Implement recommendations of the MDC studies.

Improve efficiency of Department of Statutory Bodies in monitoring parastatal operations. Prepare action plan to remove parastatal deficits and improve efficiency. Continued monitoring of MDC investments in agro-industry.

#### *C Press Holdings Limited*

Need to improve Press Holdings management, budgeting and profitability so that it can undertake new agro-industrial investments

Complete review of Press Holdings management performance, finances and corporate structure. Develop a plan for long-term financial restructuring.

Implement Press Holdings restructuring programme, adhere to new corporate guidelines, carry out studies in sale of assets.

Ensure that asset rationalisation proceeds satisfactorily.

#### *D Government Revenue*

Need to improve revenue performance to finance recurrent expenditures and local component of development expenditures, while reducing government reliance on domestic borrowing

15% increase in all specific excise and import duties, 10% hotel and restaurant tax, 3% across-the-board tariff increase to be introduced in 1981-92 budget.

Government revenue to be maintained at current ratio of GDP. License fees and tariffs to be reviewed prior to each budget. Review, and if necessary increase, public sector user charges and improve fees and charges collection systems. Improve buoyancy of tax system under IMF EFF.

Adopt a strategy towards restructuring the tax system. Introduce initial changes in 1986-87 budget.

#### *E Government borrowing*

Need to limit domestic borrowing to reduce inflation and increase private sector credit. Need to limit foreign commercial borrowing

Adhere to IMF's domestic and foreign credit ceilings. Strengthen government's ability to monitor and manage public debt.

Ensure debt monitoring system is operational. Develop borrowing strategy to achieve target 20% debt-service ratio.

Revise the external borrowing plan.

### **IV GOVERNMENT EXPENDITURE AND INVESTMENT PROGRAMME**

#### *A Recurrent expenditure*

Need to correct under-funding in agriculture and expand expenditure in key economic and social sectors in line with on-going investment programme

Commit additional MK2.8 million to agriculture in 1981-82 budget. Real growth in recurrent expenditures in key economic and social sectors during 1981-86.

Review recurrent budget allocation with Bank and ensure agricultural requirements are not under-funded.

No policy actions proposed.

#### *B Public sector investment programme*

Need to increase shares allocated to key economic and social sectors and reduce shares in low priority investments

1981-86 Public Sector Investment Programme (PSIP) to increase shares to agriculture, water, education, health and housing. Maintain share to government buildings. Provide Bank with 3-year PSIP.

Review PSIP with Bank and make necessary modification in view of changing circumstances. Prepare a PSIP for the period 1986-87 and 1988-89.

#### *C Budgetary planning*

No policy actions proposed.

Develop a system of forward budgeting with 3-year projections of revenue and expenditure by April 1984. Improve the guidelines for revenue estimates and budgetary allocation.

Update the revenue and expenditure projections to cover 1986-87 to 1988-89. Make changes to give the budget a more programmatic content.

### **V INSTITUTIONAL IMPROVEMENTS**

#### *A Economic monitoring*

Need to monitor all investments to ensure economic and financial viability

Preliminary review of all large investment co-ordinating committee and detailed review by independent consultants. Strengthen expertise in Treasury, Economic Planning Division and Ministry of Agriculture under technical assistance programme to assist with public debt, Government finance, macro and agricultural planning and statistical resources

Strengthening Economic Planning Division to assist medium-term strategy development and project identification, evaluation, monitoring and co-ordination.

Strengthen and reorganise policy-making staff of the Office of President and Cabinet and Ministry of Finance.



## Appendix 2 : Introductory statement to the in-depth interviews

*Introduction was given as follows:*

I am currently studying for a Doctorate degree at Liverpool John Moores University in Britain. My area of research is Globalisation and Structural Adjustment Programme and how they have affected Small and Micro sized enterprises in Malawi. Specific objectives are as outlined in the Conceptual Framework (here is your copy) which includes a diagram labelled Figure 1.1. In order to fit it with the framework, this interview will be centred round four main themes: Globalisation; Structural Adjustment, in particular Trade Liberalisation; Competition with regards to SMEs; and any suggestions on Strategies which you may want to propose. So what I am looking for really are your views/perceptions or comments on these subject matters. At any stage during the interview, you are free to refrain from responding or to stop the interview if you feel uncomfortable with the discussions. If you are in agreement the interview will be tape-recorded and I shall be taking some notes as well. All information recorded will be treated confidentially and not divulge to others, not even your work colleagues. No personal reference will be made in the final report and your organisation/department shall receive a copy of the report, which will contain recommendations depending on findings. Do you mind if I use the tape recorder for the discussion, as it can be too much to write notes and listen at the same time, and also to avoid missing out on some important points which you may make. (Tape-recorder turned on/off depending on response). Now, if you could please begin by giving me a brief description of your organisation/department's main activities.



## **Appendix 3: Details of governmental and NGOs for the Phase I interviews**

### *National Economic Council (NEC)*

The NEC is a government department responsible for formulating public sector investment programmes. The Council comes under the Office of President and Cabinet and is charged with developing national economic policies, which guide the economic development activities of the country. The Council initiates and coordinates the formulation and review of policies and legislation; coordinates strategic planning and budgeting process; monitors and evaluates the implementation of policies and programmes; and provides economic, statistical and information management services. Through the Poverty Reduction Strategy Paper, the NEC embarked on a new course of reducing poverty through identifying new sources of growth, which were to be promoted so as to strengthen and diversify the industrial base of the country. In the Paper, emphasis is placed upon developing a competitive industrial environment. Thus, the PRSP is a national policy document whose action plans include encouraging local manufacturers to increase the share of domestic market and encouraging synergies between local companies.

### *Ministry of Commerce and Industry (MCI)*

The Ministry's main function is to promote, support and facilitate private sector enterprise efforts in commerce, industry, micro, small and medium enterprises and cooperatives in order to make Malawi a manufacturing based economy, capable of creating and sustaining a competitive advantage in domestic and international markets. In the light of economic liberalisation programme, the role of the government in the commerce and industry sectors is now that of promoter, facilitator and coordinator, thus the MCI is the coordinating agency for government policies and programmes for these sectors. Its activities include the formulation, implementation and review of industrial policies and legislation together with coordination of spatial development initiatives and coordination of investment promotion and product development. MCI is also responsible for the formulation and implementation of internal and external trade policies and facilitating market access for Malawi's exports.

### *Regional office for Small and Medium size Enterprise Development*

This is a sub-division of the MIC, specifically set up for overseeing and developing a strategic plan for the SME sector development. It formulates and implements policies for the SME sector and coordinates the delivery of support services to the SMEs and also promotes awareness of SME opportunities, and monitors and evaluates the performance of the sector.

### *Malawi Export Promotion Council (MEPC)*

An Act of Parliament established MEPC in 1971 to provide technical assistance to registered exporters. Its function is to facilitate the development of Malawi's export trade in a bid to establish a secure foreign exchange earnings base for the country's economic development. MEPC activities include organising trade fares, product development, buyer-seller meetings, extension services to exporters and training.

### *United Nations Development Programme (UNPD)*

The main United Nations (UN) mandate is to promote sustainable human development through capacity building. Together, the Malawi government and UNDP prepared a First Country Cooperation framework for Malawi (1997-2001)



targeting sustainable livelihoods and food security, enterprise development and employment opportunities, sustainable natural resource management and the environment. At the time of the interviews, the government together with the UN was embarking on a new programme called the Enterprise Development and Employment Creation Programme, which would be part of UNDP's sustainable livelihoods programme. The programme is to focus on strengthening the development of SMEs, both to expand opportunities for employment creation and for private sector development.

#### *Malawi Investment Promotion Agency (MIPA)*

The Government of Malawi established this Agency through the Investment and Promotion Act of 1991. MIPA is a statutory body set up to promote, attract, encourage and facilitate local and foreign investment in Malawi. The Agency is charged with facilitating all aspects of investment processes in Malawi; identifying partners in or outside Malawi for joint venture business opportunities; encouraging existing investors to expand or start new investments; and making recommendations to the government regarding changes in the statutory and administrative framework relevant to the investment climate.

#### *Small Enterprise Development Organisation of Malawi (SEDOM)*

This NGO was set up in 1982 and registered as a Trust under the Trustees Incorporation Act of the Laws of Malawi. SEDOM's main functions are provision of loans, advisory services and industrial estates for micro, small and medium scale enterprises. Its main objectives include: to assist in the creation, expansion, and modernisation of Malawian-owned SMEs; to encourage Malawian entrepreneurs to use locally available raw materials to save foreign exchange; and to identify and promote SMEs with potential for exportation, import substitution and develop market for short-term lending.



## **Appendix 4: Transcript from one of the in-depth interviews**

The full interview transcript presented below was taken from some of the government officials who were interviewed by the researcher. All interviews were carried out in English, the official working language. The real identities of the officials have been kept anonymous as they were promised and assured identity confidentiality in order to protect their job positions as most of these high posts tend to be a bit political. The following is a full transcript of one of the interviews that took place:

**GM: Hello, how do you do? I am Mrs Mwandumba and thank you for agreeing to fit me in your schedule at such a short notice.**

**Mr/Mrs Y: Nice to meet you Mrs Mwandumba. Take a seat please and I must warn you I have got another appointment to attend to soon after this one. But I will try to give you as much information as I can given that we haven't got much time.**

**GM: Thank you.**

**Mr/Mrs Y: What sort of help do you require from me?**

**GM: [interview introduction as per Appendix 2] ... Do you mind if I use the tape recorder for the discussion, as it can be too much to write notes and listen at the same time, and also to avoid missing out on some important points which you may make.**

**Mr/Mrs Y: I would rather you did not tape-record the conversation if that's ok. I understand how it would help you later on but I do tend to be paranoid about tapes and cameras.**

**GM: Whatever makes you feel comfortable is fine with me. I shall just use the pen and paper and try to grasp in as much as I can. You will pardon me if I ask you to repeat some of the things you may say as I am not a fast hand-writer. Computers have spoiled some of us. Anyway, could you please give me a brief description of what your department does?**

**Mr/Mrs Y: [gives brief description of the department or organisation] Organisation/department details omitted on purpose in order to protect the respondent's identity**

**GM: Thank you, I have learned something new today. Now could you give me your views on Globalisation, what do you think about it and how do you feel it is impacting on Malawi as an economy and on the SME sector development in the country.**

**Mr/Mrs Y: First of all we need to agree on what 'globalisation' means. In my opinion it is an interaction of countries in an economic environment where you have pulls and pushes between economies through some sort of a regulatory system set out by the WTO, WB and IMF. But then within all this pushing and pulling there are losers and winners. Malawi is certainly one of those losers. What I would argue is that what we are experiencing in this country is 'internationalisation' as there is a presence of foreign corporations who transfer the assets and profits to their own countries. Malawi has not entered globalisation yet. Am I making any sense to you?**

**GM: Yes you are sir. If you could please just elaborate on the issue of Malawi not being globalised yet.**

**Mr/Mrs Y: What I mean is that to me globalisation means that certain investments made by foreign corporations are put back in the country. At the moment companies come here to make profits and leave without putting anything back, it is like some sort of exploitation since there is no tangible investment made to make our economy grow. We don't share the benefits of their assets and we can say that the level-playing field is not there.**

**GM: Ok. Now, could you please talk about what you think about the SAPs, particularly the trade liberalisation policy?**

**Mr/Mrs Y: I would like to talk about Trade liberalisation and competition together, if it's ok with you, because I think they go together. Trade liberalisation has resulted in the shrinking of the market share for the SMEs. There has been a massive increase in imports due to opening up trade barriers. These international institutions talk about SAP policies**



helping to increase productivity and efficiency in firms and that they would become more competitive, all that is not true on our part. All they wanted was a way to get in freely and make their profits from us leaving us dry and hanging. They must have known that our firms cannot compete with foreign firms. For a start the SMEs do not have the finance, capacity, competency and technology necessary to be an equal footing with the foreign companies. Human resources is not trained and as a result final products are of poor quality with a lot of mismanagement and lots of material wastes. There is no capital investment involved at all, most of them have old equipment and machinery in their factories, how can they compete as such? Many of them experience a lack financial capital and our banks are not conducive for borrowing either as the interest rates are very prohibitive. As a result of the low productivity, export growth is very minimal. Of course these SMEs do create jobs but it is just cheap labour that is not productive at all. Large domestic companies have closed down as they cannot sustain competition and retails have also closed because of competing goods coming from outside. The FDI has also been going up and down in this country because of the poor investment conditions. Transport cost is very high, inflation, interest and exchange rates are also very high. The infrastructure and corruption issues are also not helping the situation. There is too much corruption going on in this country and I don't want to mention any names or departments but it is there. All these affect the investor decisions. Another drawback of free trade is that most of the entrepreneurs in this country are involved in petty trading, all they want is an informal quick business, and how can the government generate revenue from that? I am sorry to be sounding all negative here but I can only say I am yet to see some positive impacts of the SAP policies and trade liberalisation

**GM:** Have you got any suggestions on how the country can move forward in terms of policy, assuming that some lessons have been learned from the SAPs and the situation you have just described?

**Mr/Mrs Y:** I think Malawi needs to focus on the things which it has competitive advantages on. At the moment we can say it is in agriculture. But then again, if we cannot export beyond Africa due to Developed countries protecting their markets, what hope have we got? I think we made a mistake of liberalising everything, we should have put controls on some products so that consumers could support the Malawi industry rather than buying imports at the death of our local industry. Of course for now we desperately need to find ways of increasing our exports and we also need to put some controls on foreign exchanging as we are losing money. All ministries need to work together in developing the SME sector and the government could do with coming up with ways of facilitating the survival of risk-takers. Someone needs to carry out a SWOT (strengths, weaknesses, opportunities and threats) analysis of the SMEs so that we can all focus on areas of high growth and value-adding businesses. Most emphasis in this country is on large companies, we need to start linking our SMEs with markets and large companies. The government is the biggest buyer in this country and it buys most of its goods from Asia and large companies, I think it's about time it started buying from local SMEs and this will give the SMEs much encouragement. It is easier to produce if there is a known market or buyer as it stimulates production. Anyway I should stop now otherwise I will miss my appointment. I hope I have given you a fair account of my opinion to be considered in your report and I hope I have been of help.

**GM:** Thank you very much for your time. Do you have any policy or strategy documents which you think might be of relevance to my study?

**Mr/Mrs Y:** Yes, I think there's one particular document which I think you might find very helpful. If you have a computer disk on you, you can give it to my secretary who will copy the document on the disk for you. And good luck with your research, don't forget to send us a copy of your findings.

**GM:** I shall make sure to send you a copy of the report when it is completed. It might not be the whole thesis but it will be a smaller version covering the major issues and findings. Thanks again for you time, very much appreciated and it was nice talking to you.



## **Appendix 5: Detailed responses from in-depth interviews**

### ***Statements on Globalisation***

We need to distinguish between globalisation and Internationalisation. The former is about ownership of assets and corporation in the country of business whereas the latter is about presence of an investor who later on transfers his assets and profits to their country of origin; If we agree that this is the case then I feel that Malawi has not entered globalisation as such but what is being experienced now with opening up of trade is internationalisation; Companies come and make profits and take the profits with them without re-investing in Malawi; I feel that there is more exploitation going on because the assets are not shared with the locals and there is no tangible investment to make the Malawi economy grow; With regards to globalisation, I think that level-playing field is not there; Malawi is not ready for globalisation and most SMEs do not have the necessary knowledge and skills to recognise the opportunities and benefits of globalisation.

### ***Statements on the Structural Adjustment Programme***

New government regime is encouraging laziness; People are very lazy and don't want to work. They are involved in actual farming for only a couple of months out of the whole year and yet they don't want to engage in other economic activities for the other 10 months of the year; Initiatives implemented are uncoordinated; There are no linkages between organisations and in some cases there is an element of overlap; The SAP, which was imposed by the IMF and WB, attach conditions which prevent the government from helping out or coming up its with own strategy to develop the manufacturing and production sector; Drought and suspension of aid in 1992 did not help matters either in terms of economic growth; There has been slow-down of economic growth since the SAPs. This situation will be worsened if manufacturing and industrialisation continue to be pushed aside; Manufacturing sector has lost out whereas distribution, retail and professional services are not doing too bad; There has been dis-investment in manufacturing and Malawi has been transformed from a producing to a trading economy because of the liberal trade policy; Since the number of SMEs continues to grow, they should be encouraged to lead the industrialisation process; SAP did not make a provision on how to cope with competition as many of our SMEs do not have the technology and technological know-how necessary for being competitive.

### ***Statements on Trade Liberalisation***

Exceedingly rapid trade policy reforms and dismantling of protection have led to the contraction of significant sections of the manufacturing sector; Malawi has transformed from a 'producing' to a 'trading' economy; Malawi has become a trading economy with not much of production happening. Manufacturing cannot prosper within this environment with poor infrastructure; Malawi is becoming a trading nation; There have been drops in the manufacturing of textiles and food processing due to lack of the necessary technology to produce competitive products; Most SMEs are engaged in trading which involves importing from South Africa and Zimbabwe; There is more individual trading as a result of trade liberalisation. Manufacturing and production have gone down; Productivity is very low and export growth is very minimal; There is shrinking market share for domestic firms, most goods are imports. We are even importing chicken because demand cannot be met; Increase in market share for imported goods hence cannot increase GDP; Due to problems of poverty and illiteracy, most people have gone into trading, which is a quick business. People are just buying and selling and Malawi is just consuming as a country; We cannot penetrate outside markets; Opened up too much and as a result have attracted a large influx of imports and cheaper goods; Imported goods are cheaper for individuals; Imports are coming in cheaper; Government has only just started registering small companies through



Ministry of Commerce and Trade, but most of them are not taxed, there is no law for small-scale taxing; There is a disintegration of macro businesses which is underestimating GDP; The informal trade has resulted in loss of government revenue; Trade liberalisation has not been managed well. There is no policy and strategy to manage the trade liberalisation process. We need to draw lessons from this; Trade liberalisation was imposed on Malawi by Bretton Woods, and they did not mention the negative side of it when they were encouraging it; I feel that Trade liberalisation was imposed on the government by World Bank and IMF whereas the government has got its own concepts which it cannot exercise at the moment; We have been forced to come up with poor domestic policy by WB/IMF, policy which suppresses industrial competence and there is no subsidy to farmers; Production, which is in decline, creates employment; There is limited access to foreign markets and people need to be trained on how to access these markets but there is no money for this; There have been problems with management of the economy; Government expenditure has had major impact on local businesses; There are not enough funds for private sector to borrow from the banks since banks have lent chunks of money to the government which is failing to make the appropriate repayments; High inflation and interest rates have affected businesses – cost of capital is very high; As regards to benefits of free trade, it depends on which sector: manufacturing sector has lost out whereas distribution, retail and professional services have gained; There are only a few export commodities which are mainly agricultural. There are a few exports to South Africa, and there is an ongoing dispute over export volumes to Zimbabwe. Potential export products include textiles, small-scale mining and tourism, the potential which we are not maximising due to out-of-date machinery; Malawi has been given a quota to export textiles to USA but we are failing to do so because the textile we produce is of poor quality and the production process is very slow due to obsolete machinery and frequent electricity power cuts; Malawi hotels are not doing very well in attracting tourists or even locals. It is all about pricing methods which nobody has a clue how they come up with them. They are very expensive hotels and as a result very few tourists stay in them; There is not much to export. Last year imports were worth \$1 billion compared to \$400 million worth of exports and most imports are luxuries which the country can do without; Not much is exported by the SMEs; I think there has not been noticeable positive impacts as far as opening up trade is concerned; In terms of exports, volume of other products has grown and others have retreated; There have been gains and losses in different areas and we need to refocus on where there has been an increase; Domestic industries say they are not ready for liberalisation and are crying foul; Some local businesses feel that incoming investors have been given preferential treatment; They should not have liberalised everything. We should have some protection on key items and just control on quality; There are no safeguards for domestic market, maybe the country rushed in with liberalisation; As far as international trade agreements are concerned, there is not much consultation with technical people and they don't even look at the level of our SMEs. The government has not considered inclusion of factors which impact negatively on SMEs; There is no control on foreign exchange as a result the country is losing money; Domestic demand is being satisfied through import of goods and services hence deficit on balance of payments. And this may lead to more borrowing and debts.

### ***Statements on Competition***

Cheaper imported commodities which are competing with local enterprises. Competition is very strong and it is mainly in terms of quality and packaging; Malawi's low manufacturing capability has raised the domestic market share for the imported manufactured goods up to 95% this year (2002); Large enterprises like Press Bakeries have collapsed. Now you find a lot of family level bakeries and shop bakeries; BAT, the manufacturer of cigarettes, has also collapsed and all the cigarettes are being imported although the tobacco is grown here. It is cheaper for consumers though; David Whitehead, the textile manufacturer is on the verge of collapsing; Shire Bus service company, the large public transport provider, is also collapsing due to emergence of so many individual private mini-bus services who are not



taxed at all and the government is losing out. The bus company has tried aggressive marketing but it is not working; Canned factory food processing company has also collapsed; Loss of jobs in the formal sector due to companies shutting down; Producing companies are closing down and trading is increasing due to competitive world economy; Medium-sized businesses are being taken over or going into liquidation due to financial difficulties; Companies have had to close due to competition brought about by trade liberalisation. Retail shops have had to close due to competitive goods coming from outside the country; Big companies are reducing operations in Malawi; Most companies used to be monopolies hence not geared for competition as they only had the Malawi market and not many of them had to face the outside market competition; Industries here are not well equipped for competition. Transport cost is too high for most of them and they also use obsolete technology; Domestic market is small; There are a lot of infrastructure problems such as electricity, water services and roads are very poor and this impacts on productivity; There is no capacity and necessary technology and infrastructure to produce competitive products and thus cannot take up the opportunity of free trade and cannot access foreign markets; Competition is there but it is not fair because it is about capital, competency and technology, which Malawi firms do not have. There is lack of modern technology and they have obsolete factories and equipment; Local products are uncompetitive due to high transport costs (Malawi being a landlocked country), obsolete technologies and poor infrastructure. For instance, the internal road network is well below standard; There is poor infrastructure and out of date technology and the country cannot compete like that; There has been ups and downs with regard to Foreign Direct Investment due to poor economic environment made up of high transport costs; poor infrastructure; high inflation, interest and exchange rates which all affect investors decisions; We don't have very competitive local products due to poor quality, packaging and marketing. People don't have information on market share and have no knowledge of competitors; We need to concentrate on things which Malawi has competitive advantage on; There are small production units which cannot meet the demands; We need to address SME constraints. Look at strengths, weaknesses, threats and opportunities, and then focus on areas of high growth; Crime has gone up considerably and this has become a problem for businesses because they end up spending a lot of money on security; Government needs to do something to facilitate survival of risk-takers; Adequate financial resources should be allocated to a sector responsible for small enterprises and entrepreneurship should be encouraged; Value adding to products is very minimal in Malawi; Due to low quality, the tobacco prices are being depressed; Less value is attached to local products; We need value-added products in order to bring foreign exchange into the country. And for value-adding, we need capital, which is not easy to raise due to high interest rates; In terms of financial capital, banks are not conducive for borrowing companies since interest rates are very prohibitive hence local companies cannot compete; There is no doubt that high tariffs, restrictive measures through policy, law and admin arrangement and other non-tariff measures impede exports, but the question is 'can Malawi compete on the international scene?'; Local firms were not given enough time to increase their competitiveness and as a result are losing out to competition from imports; There is no inter-industry linkage, for example some SMEs import raw materials instead of using own local materials; There are no linkages between SMEs and large companies. It will be easier for SMEs to be motivated to produce if there was a known market for them; Human resource is not trained and as such final products are of poor quality and there is mismanagement and a lot of waste in production; There is a lot of unproductive cheap labour; There isn't much foreign investment due to lack of proper human resource; There is no emphasis on entrepreneurship. People don't understand issues of entrepreneurship and globalisation. With the lack of knowledge in accounting of finances, no discipline of business mind, they end up using all capital on personal needs; Competition is very stiff these days and not many firms are surviving within this environment. It is especially tough for the industrial sector and manufacturers; No studies have been carried out on how competitive Malawi enterprises have become due to free trade; Most local companies now



know that quality is important and only the efficient enterprises will survive; The new Poverty Reduction Strategy Paper is becoming too late as half of the population is below poverty line; The Poverty Reduction Strategy recognises SMEs as critical stakeholders; As competition policy has now been drafted, hopefully there will be an improvement on things; Marketing of the country and products needs to be done vigorously so that people can be encouraged to engage in production; In terms of agriculture, there is a need for diversification as World Health Organisation has given the country less than five years to stop producing tobacco, which is the major export product; Some form of intervention by the government is required in some selected sectors such as the textile industry.



## Appendix 6: List of Documents obtained from In-depth interviews

• Malawi Poverty Reduction Strategy Paper, Malawi National Economic Council	2001
• White Paper on Strategies for enhancing the growth of Micro, Small & Medium Scale Enterprise in Malawi, Ministry of Commerce and Trade	2000
• Enterprise Development and Employment Generation Programme 1997-2001, Ministry of Commerce and Trade	2000
• Strategic Plan 2001-2004, Ministry of Commerce and Trade	2001
• Towards Competition Policy in Malawi: A Situation Analysis, Ministry of Commerce and Trade	1995
• Integrated Trade and Industry Policy, Ministry of Commerce and Trade	1998
• The Malawi Products Handbook, Malawi Export Promotion Council	2000
• Investors Guide to Malawi, Malawi Investment Promotion Agency	2002
• The Impact of Trade Policy Reforms on Malawi's Manufacturing Sector, World Bank	2000
• Directory of Micro, Small and medium Enterprises Products in Malawi	2001
• Malawi: Globalisation, Liberalisation and Sustainable Human Development	2000
• Country Assessment Report, UNDP/UNCATD	1999



## Appendix 7: Questionnaire

### Questionnaire on Globalisation, Structure Adjustment Programme and Impact on SMEs

#### *Explanation to the Interviewee:*

This investigation is being carried out by a research student from Liverpool John Moores University in the order to obtain more information about opportunities and threats brought about by globalisation and structure adjustment reform measures. The purpose of this interview is to gather views and problems faced by SMEs in Malawi as well as personal situations of entrepreneurs with regards to the economic reforms. This information should assist those in responsible positions for SME development in their attempt to improve and develop the sector. Would you mind if I asked you a few questions regarding your business? You can be as critical as you want in your answers because you will remain anonymous, and you are not obliged to respond to any questions that do not feel comfortable with.

Questionnaire No..... Date of Interview.....

1. District  
 2. Name of town/village.....  
 3. Category

1 Zomba      2 Blantyre      3 Other  
 1 Rural      2 Urban

#### I Characteristics of Entrepreneur

4. Sex of Interviewee  
 5. In what year were you born?.....  
 6. What is your marital status?.....  
 7. What is your level of Education?.....  
 8. Have you ever had any training relevant to entrepreneurial skills? 1 Yes 2 No  
 If Yes, what kind of training did you have?.....  
 9. Do you have any knowledge regarding changing technology and markets?  
 Please comment on your answer.....  
 10. What is your occupation? .....  
 11. Have you ever worked as a civil servant in the last 10 years? 1 Yes 2 No  
 If Yes, why did you leave your employment?.....  
 12. Apart from running your own business, are you currently employed elsewhere? 1 Yes 2 No  
 If Yes, what kind of employment do you have?.....  
 13. Are you currently looking for other employment? 1 Yes 2 No  
 If Yes, would you please give a reason for why.....  
 14. What motivated you to start up your own business?.....  
 15. Are you a member of any business group/association? 1 Yes 2 No  
 If Yes, please specify.....

#### II Enterprise Characteristics

16. What type of business do you have?.....  
 1 production      2 trade      3 service



17. Who owns the business?.....  
 1 husband      2 wife      3 both      4 joint with other partners      5 limited co.  
 6 other (please specify).....
18. Number of employed staff (including owner).....  
 1 1-4      2 5-20      3 21-50      4 51-99      

small	medium
-------	--------
19. When was your enterprise created?.....  
 1 before 1981      2 between 1981 and 1988      3 between 1988 and 1994      4 after 1994
20. Is your business registered with Ministry of Commerce & Industry?      1 Yes      2 No  
 If No, why not.....
21. If 'No' to Q20 above, do you see your business graduating from informal to formal status?  
 1 yes, in two years time      2 in a few years time      3 don't know      4 no  
 Please comment on your answer.....
22. Do you have any plans to expand your business from small to medium or medium to large?  
 1 yes, in two years time      2 in a few years time      3 don't know      4 no  
 Please comment on your answer.....

### III Operating Environment

#### A. Business Operations

23. Where do you carry out your business operations?  
 1 home      2 own business premises      3 rented premises  
 4 other (please specify).....
24. Where do you purchase your raw materials or goods if in trading?.....  
 1 other local entrepreneurs      2 town centre      3 other districts      4 other countries  
 If buying from abroad, please state why?.....
25. Who are your main clients?.....  
 1 rural population      2 low income urban population      3 high income urban population  
 4 both rural and urban population      5 large companies      6 tourists      7 vendors/traders  
 8 stalls/shops      9 other SMEs      10 other (please specify).....
26. Who are your main competitors?.....  
 1 other small enterprises      2 large enterprises      3 both small & large enterprises  
 4 imports      5 none      6 other (please specify).....
27. Is there enough demand for your products?  
 1 more than enough      2 about right      3 not enough  
 Please comment.....
28. If you were to increase on current production, could you sell more?      1 Yes      2 No  
 If No, please give reasons.....
29. Would you be able to produce more if demand increased?      1 Yes      2 No  
 If No, why?.....  
 1 working capital      2 storage infrastructure      3 price fluctuations  
 4 transport difficulties      5 problems in obtaining raw materials      6 other (please specify).....
30. Have you invested in new equipment/machinery in recent years?      1 Yes      2 No  
 If Yes, please specify what.....  
 If No, please give reasons.....
31. If you make your own products, have you modernised the means of production?      1 Yes      2 No  
 If No, please give reason.....
32. Do you normally have business dealings with other local entrepreneurs?  
 1 frequently      2 sometimes      3 never  
 If never, why?  
 1 not acquainted yet      2 do not trust them      3 they are direct competitors      4 other  
 Please comment on your answer.....  
 If frequently or sometimes, what sort of business support do you offer one each other (tick as many as apply)  
 1 lend each other finances      2 help with some work      3 exchange business ideas  
 4 moral support      5 other (please specify).....
33. Do you sale or exchange your products/goods with other entrepreneurs?  
 1 frequently      2 sometimes      3 never  
 Please comment on your answer.....



34. Do you feel isolated in terms of contact with other entrepreneurs?  
 1 most of the times                      2 sometimes                      3 never  
 Please comment on your answer.....
35. Do you have any associations or dealings with large enterprises?  
 1 frequently                      2 sometimes                      3 never  
 Please comment on your answer.....
36. What would you say were the three main difficulties constraining your business operations?  
 Please list in order from the most to the least constraint:  
 1.....  
 2.....  
 3.....  
 Please comment on your answer.....
37. Do you see your business operations growing/expanding in the next few years?  
 1 yes, will expand    2 no, will remain as it is                      3 looking to wind down soon                      4 don't know  
 Please comment on your answer.....
38. Do you, as a business, export your products?                      1 Yes                      2 No  
 If No, why?.....
39. If No to Q39 above, would you be interested to export your products?                      1 Yes                      2 No

#### *B. Infrastructure*

40. What means of transport do you normally use for running business errands?  
 1 walk                      2 private minibus                      3 matola (hitch hiking)                      4 bus service  
 5 own car                      6 bicycle/motorbike                      7 ox cart                      8 hiring vehicles  
 9 other (please specify).....
41. Do you consider transport costs to be:  
 1 very high                      2 high                      3 fairly reasonable                      4 reasonable  
 Please comment on your answer.....
42. Is transport a problem for you?  
 1 a serious problem                      2 problem but not a very serious one                      3 not a problem  
 Please comment on your answer.....
43. Is water supply a problem for you?  
 1 a serious problem                      2 problem but not a very serious one                      3 not a problem  
 Please comment on your answer.....
44. Do you use electricity for business operations?                      1 Yes                      2 No  
 If No, why not?.....
45. Is electricity supply a problem for you?  
 1 a serious problem                      2 problem but not a very serious one                      3 not a problem  
 Please comment on your answer.....

#### *C. Finance*

46. Where did you get capital for starting up the business?  
 1 bank/building society loan                      2 credit union                      3 saved up from employment  
 4 relatives/friends                      5 redundancy/retirement money                      6 other (specify).....
47. How easy or difficult is it to obtain credit from formal financial institutions?  
 1 very difficult                      2 quite difficult                      3 quite easy                      4 very easy  
 Please comment on your answer.....
48. How easy or difficult is it to access finance for business growth/expansion these days?  
 1 very difficult                      2 quite difficult                      3 quite easy                      4 very easy  
 Please comment on your answer.....

#### *D. Regulatory Environment*

49. Were you required to obtain government permission to start your business?                      1 Yes                      2 No  
 Please comment on your answer.....
50. Do you pay any form of tax?                      1 Yes                      2 No  
 If Yes, please specify.....
51. Do you have to comply with any government laws/regulations in your business operations?                      1 Yes                      2 No  
 If Yes, please elaborate.....



52. Do you have to meet certain standards of quality for your products? 1 Yes 2 No  
Please comment on your answer.....

53. Where do you sell your products/merchandise?.....  
1 central market 2 from home 3 commercial/industrial district  
4 roadside 5 mobile 6 other (please specify).....

54. Are you restricted by the government on where you can sell your merchandise? 1 Yes 2 No  
Please comment on your answer.....

55. Do you find the regulatory environment restrictive or not to business initiatives?  
1 very restrictive 2 quite restrictive 3 quite unrestrictive 4 very unrestrictive  
Please comment on your answer.....

56. How easy or difficult is it to obtain information on marketing or available business support?  
1 very difficult 2 quite difficult 3 quite easy 4 very easy  
Please comment on your answer.....

57. If involved in exporting or importing, do you find customs & excise:  
1 very bureaucratic 2 inhibiting 3 easy to deal with  
Please comment on your answer.....

58. What are the main difficulties imposed by the regulatory environment?.....  
.....

59. Any suggestions about what you would like to see happen regarding:  
Government Support.....  
Other Institution Support.....  
Regulatory environment.....

60 In general, what would you like to see happen to enhance your business growth?.....  
.....

**IV. Satisfaction & Problems with enterprising life**

61. How satisfied are you with the way your business is performing at the moment?  
1 very dissatisfied 2 dissatisfied 3 neither satisfied nor dissatisfied 4 satisfied 5 very satisfied  
Please comment on your answer.....

62. Which of the following statements can you identify yourself with most?  
1 life in business is very difficult for me these days  
2 life in business is difficult  
3 neither easy nor difficult  
4 easy for me  
5 very easy for me

63. What would you say is the main problem affecting your business operations at the moment?.....  
1 transport 2 can't get a loan 3 high interest rates for loans 4 competition  
5 water supply 6 lack of market 7 procuring raw materials 8 low demand  
9 obsolete technology 10 other (please specify).....  
Please comment on your answer.....

64. What is the second problem affecting your business operations (use above codes)?.....  
Please comment on your answer.....

65. What is the third problem affecting your business operations (use above codes)?.....  
Please comment on your answer.....

66. Over the past years, when would you say that enterprising life was most difficult for you?.....  
1 before independence 2 right after independence until about 1981  
3 between round 1981 and 1994 4 from 1994 up to 1999 5 now  
Please comment on your answer.....

67. During the last 10 years:  
1 business has improved in many ways  
2 business has improved in some ways  
3 for me business did not change much after 1994  
4 business has become more difficult  
Please comment on your answer.....

68. How do you think life in business will change in the next few years?  
1 will improve 2 will not change much 3 will become worse  
Please comment on your answer.....



## V Impact of the Adjustment Programme

69. When were you aware that trade restrictions had been lifted by the government?.....  
 1 since 1981      2 since 1988      3 since 1994      4 about 1995      5 not aware  
 6 can't remember
70. Describe the main changes recorded since the start of your business in terms of:  
 1 Production.....  
 2 Employment.....  
 3 Investments.....  
 4 Product range.....  
 5 Imports & exports.....
71. Since the domestic deregulation, has it been easy for your business operations?.....  
 1 very difficult      2 difficult      3 no change      4 easy      5 very easy      6 not sure  
 Please comment on your answer.....
72. Since trade policy reforms, how easy is it to find funds for financing new equipment?  
 1 very difficult      2 difficult      3 no change      4 easy      5 very easy      6 not sure  
 Please comment on your answer.....
73. Since opening up the market to foreign trade, is the market share for your business:  
 1 shrinking      2 expanding      3 no changed      4 not sure
74. Since the exchange rate reforms, are you able to access foreign markets for your products/goods?  
 1 Yes      2 No  
 If No, why not?.....  
 If Yes, have you experienced an increase in foreign market opportunities since trade liberalisation?  
 1 decrease      2 no change      3 increase
75. How competitive do you think your products are or would be on the international market?  
 1 very competitive      2 competitive enough      3 not competitive enough      4 do not stand a chance  
 Please comment on your answer.....
76. How competitive do you think your products are on the domestic market?  
 1 very competitive      2 competitive enough      3 not competitive enough      4 do not stand a chance  
 Please comment on your answer.....
77. In your opinion, what would it take to make your products more competitive both abroad and at home?  
 .....
78. Since fiscal & monetary reforms, how easy is it to obtain raw materials from abroad?  
 1 very easy      2 easy      3 same as before      4 difficult      5 very difficult      6 not tried it  
 Please comment on your answer.....
79. Since exchange rate reforms, can you afford equipment at appropriate technological level?      1 Yes      2 No  
 Please comment on your answer.....
80. After trade liberalisation, the number of customers buying from you has:  
 1 increased      2 decreased      3 not changed      4 not sure  
 Please comment on your answer.....
81. Since domestic deregulation, are your prices competitive?  
 1 not competitive      2 competitive      3 no change      4 very competitive      5 don't know  
 Please comment on your answer.....
82. Since price liberalization of crops, has demand for your products:  
 1 decreased      2 increased      3 remained the same?  
 Please comment on your answer.....
83. Has productivity/output increased in your business since trade liberalisation?      1 Yes      2 No  
 Please comment on your answer.....
84. Have new areas of economic activity been opened up for you by trade liberalisation?      1 Yes      2 No  
 Please comment on your answer.....
85. Is your enterprise more profitable now than before?      1 Yes      2 No  
 Please comment on your answer.....
86. Do you think you are well equipped to compete globally?      1 Yes      2 No  
 Please comment on your answer.....
87. Do you see your business growing due to free trade?      1 Yes      2 No  
 Please comment on your answer.....



88. The following have been mentioned, in previous similar surveys in Malawi, as main factors inhibiting competitiveness of local products. Please tick whether you agree or disagree in each case.

	1 poor roads	2 high transport costs	3 obsolete technology	4 high interest rates
Strongly disagree				
Disagree				
Neither agree nor disagree				
Agree				
Strongly agree				

Any other factors in your opinion?.....

VI Response to Adjustment Measures

89. How did you respond to the incentive mechanism brought about by trade reform measures?

1 diversified outlets	2 sought export markets	3 product diversification
4 invested in advanced equipment	5 that's when I started the business	6 no change

Please comment on your answer.....

90. Do you import your raw materials? 1 Yes 2 No

If Yes, have you reduced or increased your share of imported raw materials?

1 reduced	2 same	3 increased
-----------	--------	-------------

Please comment on your answer.....

91. What strategies have you come up with to enhance your product competitiveness?

.....

92. What do you see as the main hindrance to your strategy for business development?

.....

93. Would you consider working with other SMEs to strengthen your position in the domestic market? 1 Yes 2No

If No, why not?.....

94. Any general comments in addition to the above points?.....

.....