Foreign Trade Potential, Small Enterprise Development and Job Creation in Developing Countries

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ABSTRACT. Increasing American competitiveness in the international economy requires expanding trade with emerging markets, especially in developing countries of Asia, Latin America and Africa. Historically, as developing countries' economies have grown, the capacity for exporting and importing have both expanded. In the future, the capacity for trade in developing countries will depend increasingly on their ability to create sufficient numbers of jobs to absorb their rapidly growing labor forces.

Unlike Western countries, most developing economies have a small percentage of their labor forces in large-scale manufacturing and a large share engaged in small-scale and informal sector enterprises. Small-scale enterprises have been the primary sources of labor absorption in cities in developing countries and will continue to play a crucial role in the future. Experience has shown that policies for improving the capacity of small-scale enterprises to generate jobs have had only mixed results in developing countries. The challenge facing governments and the private sector in the future include: (1) creating an economic environment conducive to small-enterprise development; (2) removing regulatory and administrative obstacles to small-enterprise expansion; (3) tailoring small-enterprise promotion programs to local conditions and needs; (4) providing capital and credit for small-business owners; (5) involving the private sector in small-enterprise development programs; and (6) providing technical assistance, training and educational programs through public-private partnerships.

Improving the United States' balance of trade is a high priority of American economic policy. Achieving this goal will require American companies not only to compete more effectively in the domestic market and in Europe and Japan, but also to expand their exports to emerging markets. Developing countries, which consumed less than one-third of U.S. exports in the past, are poised to provide substantial new export opportunities.

The trends are clear. U.S. merchandise exports to developing countries increased from $74.4 billion in 1984 to $127.4 billion in 1990. Mexico has already become the third largest market for U.S. merchandise exports, moving ahead of the United Kingdom and just behind Japan. In 1991, the United States exported nearly $30 billion in merchandise to Mexico. The four Asian newly industrializing countries (NICs) — South Korea, Taiwan, Hong Kong and Singapore — together accounted for over $40 billion in exports. American companies also sold larger amounts of goods to Brazil, China, Malaysia, Venezuela and Thailand. (See Table I.) Exports to the Caribbean Region grew by 6 percent from 1989 to reach $9.3 billion in 1990, while exports to members of the Association of Southeast Asian Nations (ASEAN) increased by 18 percent to nearly $19 billion (U.S. Department of Commerce, 1991).

At the same time, the United States had a significant trade deficit with all but about a dozen developing countries in 1990. The ability of American companies to expand exports to developing countries in the future will depend on these countries' overall level of economic growth, particularly on their ability to expand their internal markets. Although economic development strengthens the capacity of countries to increase their exports and to create import-substitution industries, countries with the strongest economic growth have generally had the highest average annual import growth rates. From 1980 to 1988, imports grew on average by 6.9 percent a year in East Asia, for example, and by 4.4 percent in South Asia. In

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Latin America and Sub-Saharan Africa, which suffered serious economic setbacks during the 1980s, imports declined.

Economic growth leading to higher levels of trade by developing countries creates both export and import opportunities. In South Korea, for example, economic development was based on export promotion, but its import share of GNP increased from 25.4 percent in 1968 to 30.4 percent in 1985 (UNIDO, 1987). Among the developing countries to which the United States exported more than $1 billion in merchandise in 1990, overall capacity to import grew substantially between 1973 and 1989. Import capacity increased nearly four-fold in Mexico, five-fold in Malaysia and six-fold in Turkey. It increased by more than 750 percent in Thailand, 900 percent in Indonesia and 1,500 percent in China and 7,000 percent in South Korea. (See Table I.)

TABLE I
U.S. merchandise exports to, and import capacity of, selected developing countries

Country	U.S. merchandise export value F.A.S. (billions of dollars)		Capacity to import (millions of LCUs)		
	1980	1990	1973	1989	Percent change
Mexico	15.1	28.4	8,100	40,373	+ 398
South Korea	4.6	14.4	675	51,264	+7494
Taiwan	4.3	11.5	—	—	—
Singapore	3.0	8.0	—	—	—
Hong Kong	2.7	6.8	—	—	—
Brazil	4.3	5.1	—	—	—
China	3.8	4.8	13	216	+1561
Malaysia	1.3	3.4	10,306	64,454	+ 525
Venezuela	4.6	3.1	—	—	—
Thailand	1.3	3.0	68	582	+ 755
Philippines	1.9	2.5	62	244	+ 293
India	1.7	2.5	96	262	+ 173
Turkey	0.5	2.3	1,898	14,130	+ 644
Egypt	1.9	2.2	12,135	7,225	− 40
Colombia	1.7	2.0	436	1,557	+ 257
Indonesia	1.5	1.9	3,388	35,050	+ 934
Chile	1.4	1.7	125	371	+ 196
South Africa	2.4	1.7	—	—	—
Pakistan	0.6	1.1	38	81	+ 113
Algeria	0.5	0.9	21,571	42,065	+ 95

Sources: U.S. Department of Commerce (1991); IMF (1987); World Bank (1990).
F.A.S. = Free Alongside Ship.
LCUs = Local Currency Units (at constant 1987 prices).

Future internal market growth in developing countries will depend, in large part, on expanding employment for their rapidly growing labor forces in order to raise consumer incomes and aggregate purchasing power. Failure to create sufficient numbers of jobs will widen the economic gap between more developed and less developed countries and could lead to social and political tensions that diminish export and investment prospects of U.S. companies in developing regions.

American trade policies, and the strategic plans of multinational corporations, often overlook or discount the dramatic demographic changes occurring in developing countries that will influence the size and location of potentially lucrative export markets. During the next 35 years, the economically active population in developing countries will increase by over 1.2 billion, with almost all growth occurring in cities (International Labour Organization, 1986; Rondinelli and Kasarda, 1990). Accompanying this growth will be the continuing restructuring of Third World economies from agriculture to manufacturing and services. One of the most critical challenges confronting developing countries, therefore, will be to create enough jobs for the massive growth projected in their labor forces, especially in urban areas.

Shortly after the turn of the century, more than half of the labor force in developing countries will be in non-agricultural occupations and more than half will be working, or seeking work, in urban places. Of the 3 billion total population increase expected in developing nations between 1990 and 2025, 87 percent will be in urban places (United Nations, 1989). The number of people who will be living in Third World cities will reach nearly 2 billion at the end of this decade and will double to 4 billion the following 25 years (UNCHS, 1987). Assuming that the location of the economically active population will be distributed between rural and urban areas in approximately the same proportion as the general population, the size of the labor force in urban areas is likely to double from about 409 million in 1980 to more than 839 million in the year 2000. It will double again to 1.7 billion by 2025.

These computations, illustrated in Table II, suggest that more than 228 million new jobs must be created in urban areas in developing countries during the 1990s to sustain economic growth and

TABLE II
Estimated urban labor force growth in less developed countries (assuming labor force distributed in proportion to urban-rural population distribution), 1990—2025

	1990	2000	2010	2020	2025
Less developed countries					
Number of economically active population (millions)	1778.0	2137.7	2510.8	2862.8	3012.6
Percent of population in urban areas	33.6	39.3	46.2	53.1	56.5
Size of urban labor force (millions)	597.6	839.7	1158.7	1521.0	1701.2
Africa					
Number of economically active population (millions)	242.8	318.3	425.4	565.9	649.6
Percent of population in urban areas	32.7	39.1	45.7	52.3	55.4
Size of urban labor force (millions)	79.4	124.5	194.4	295.9	359.9
Latin American and Caribbean					
Number of economically active population (millions)	293.7	346.5	401.9	446.7	465.8
Percent of population in urban areas	72.0	76.8	80.1	82.9	84.1
Size of urban labor force (millions)	211.5	266.1	321.9	370.3	391.7
Asia					
Number of economically active population (millions)	1374.3	1616.2	1835.3	2003.4	2050.4
Percent of population in urban areas	29.9	34.9	41.9	49.3	52.8
Size of urban labor force (millions)	410.9	564.1	768.9	987.7	1082.6

Source: United Nations, 1988.

expand internal markets. An additional 875 million jobs will be needed during the following 25 years. To absorb the enormous growth of the urban labor force, at least 280 million new jobs must be created in cities and towns in Africa, 180 million in Latin America and the Caribbean, and almost 672 million in Asia.

The downside implications of such demographic changes, however, lie in the fact that to date, most developing countries have not been able to increase investment, production, and jobs at a rate equal to or higher than urban labor-force growth. Even developing countries that have experienced relatively strong economic growth have faced problems providing sufficient numbers of jobs. Recent studies indicate that unemployment in Latin American cities increased during the 1980s (Tokman, 1988). In many African countries, the rates of open unemployment in cities dramatically expanded (McNulty and Adalemo, 1988). Underemployment is also a serious problem with as much as 40 percent of the workplace in many Third World cities underemployed (van Ginneken, 1988).

Generating the needed numbers of jobs to raise incomes and strengthen internal markets will require innovative policies that hasten the development of small-scale enterprises. Although large- and medium-scale manufacturing firms have contributed an impressive number of jobs in the newly industrializing countries of Asia, they have absorbed only a modest portion of urban labor force in other developing countries. Most urban jobs are being created by small commercial and service enterprises, a majority of which are in the informal sector (Edgren and Muqtada, 1989). These "informal sector" enterprises are primarily family-operated or individual activities that are not legally registered and usually do not provide employees with social security or legal protection. But they support more than half of the labor force in many large cities, and from 70 to 90 percent in secondary cities and small towns (Rondinelli, 1983; Rondinelli and Kasarda, 1990).

In the sections that follow we elaborate on the important role of small enterprises in urban job creation and market expansion that will affect the prospects of developing countries engaging more actively in international trade in the future. Based on lessons from experience, we then identify policies and programs that would increase the job-creation potential of small urban enterprises and ways that the private sector can further promote their expansion.

The crucial role of small-scale enterprises

The role of small-scale and informal enterprises in absorbing labor is a matter of continuing debate in both more developed and less developed countries. Birch's (1987) contention that small businesses are primary sources of job creation has been challenged by some labor market analysts (Storey and Johnson, 1987; Brown *et al.*, 1990; Little, 1987). Yet, a significant amount of empirical research supports the thesis that small businesses provide a large number of jobs in Western societies (Acs and Audretsch, 1989); and they are not only the most important source of livelihood for urban households in developing countries, but they also are crucial for social mobility, economic sustainability and market expansion (Ashe, 1985; Fields, 1990). These enterprises provide women and children opportunities to supplement household income; they offer poor and middle-class families essential goods and services; and they give technical and entrepreneurial training to urban workers. In addition, small enterprises mobilize savings for people who lack access to formal credit (Portes *et al.*, 1989). They survive in urban areas because they use a favorable mix of capital, labor and energy, and have commercial links to modern manufacturing. In most urban areas, small businesses seem to be resilient even when national economies experience difficulties.

The rise of large- and medium-scale manufacturing in many developing countries has not diminished the importance of small enterprises. Despite rapid industrialization in Latin American countries from the 1950s through the 1980s, for example, the portion of the labor force employed in micro enterprises declined by less than 0.05 percent. Micro-enterprises still employ about 30 percent of the economically active population in Latin America. If wage laborers in enterprises that do not offer social security and other forms of labor protection are counted, the portion of the total labor force in the informal sector increases to about 50 percent (Castells and Portes, 1989).

Even in the Asian NICs, where growth in manufacturing jobs has been relatively high, it has been small- and medium-sized enterprises in the services sector that have absorbed the largest portion of the employed labor force — about 50 percent in South Korea, 62 percent in Hong Kong, and 73 percent in Singapore — from the mid-1970s to the mid-1980s (Edgren and Muqtada, 1989). The "organized" formal sector in poorer Asian countries has been able to absorb only a small percentage of the annual labor-force growth: about 5 percent in Bangladesh, for example, and 10 percent in India.

Small enterprises as urban job generators

Small enterprises, as job generators, are not confined to service activities. In South Asian countries — India, Bangladesh and Pakistan — at least 80 percent of the total manufacturing employment is accounted for by small-scale and cottage industries; in the poorest countries, like Nepal, they account for as much as 96 percent (ILO-ARTEP, 1987). For these and other poor countries, small enterprises provide the vast majority of goods-producing jobs, most of which are found in cities.

Many small enterprises in Third World cities engage the labor of from one to three family members and sometimes one or two full- or part-time employees (Cohen, 1984a). In Bogor, Indonesia, one of every sixteen residents is involved in some aspect of street food enterprise (Cohen, 1984b). In Dar es Salaam, food shops require two full-time operators or several part-time employees. Many of the shops, however, are run by several members of the same family working part-time on different days of the week or at different times of the day. Informal-sector enterprises in Davao City, the Philippines, operate with about three people each, and some sellers in market places hire part-time help for specific tasks (Barth, 1984).

The number of urban residents who depend directly on informal-sector activities for all or part of their income can be four to six times the number of such activities within a city. The number of people who depend indirectly on income from informal activities — if formal-sector suppliers are taken into account — can be as high as 10 times the number of informal-sector participants (Rondinelli, 1987).

Moreover, as noted above, many small enterprises in Third World cities, such as food vending and preparation activities, are operated by women and provide a source of employment that supplements the income of other family members. Indeed, sale of household goods, food marketing, street food preparation and selling and similar occupations are dominated by women in many Asian and African countries. Studies of street food vendors in Ziguinchor, a secondary city in Senegal, reveal that 77 percent are women (Cohen, 1984b). Surveys of the street foods sector in Iloilo, the Philippines, indicate that 80 percent were female and that women were the dominate partners in activities operated by both husbands and wives (Barth, 1983).

Small-scale and micro-enterprises employ more than 70 percent of the labor force in Indonesia (Demographic Institute, 1989a). In 1985, nearly 45 percent of workers in Indonesia were either individually self-employed or assisted by family members; an additional 24 percent were family workers. Micro-enterprises are the main source of jobs for unskilled laborers who migrate to urban areas and for those who shift from agricultural to non-agricultural occupations in rural areas. Because of ease of entry, low capital investment requirements, and low skill demands, small enterprises such as street trading, food preparation, and hawking and vending offer a survival mechanism for the urban poor and for new migrants to Indonesian cities and towns. Small-scale transportation services, stall-selling activities, mobile vending operations and low-cost service provision all employ large numbers of Indonesia's city dwellers (Demographic Institute, 1989b).

Small enterprises are not just temporary sources of employment for Indonesia's urban workers (BPPN *et al.*, 1987). Studies of food-vending enterprises in Jakarta, Semarang and Samarinda show that, although more than 70 percent of the respondents were migrants, the majority had been involved in small enterprises at their current location for more than 10 years. Moreover, informal-sector employment was perceived by the majority of the 280 respondents as a permanent occupation. More than 68 percent of the street traders had never applied for formal-sector jobs. The majority in Jakarta and Semarang operated at fixed locations. Over 90 percent owned their own businesses. Most of the respondents were satisfied with the income derived from their activities: only 4 percent considered themselves poor; 86 percent believed they derived sufficient income from their activities to consider themselves moderately well off. Net income for most street vendors was more than the official minimum wage. About 37 percent of the sample surveyed in Jakarta, Semarang and Samarinda reported having at least one employee and 15 percent had two or more employees (BPPN *et al.*, 1988).

The economic structure of secondary cities and towns in developing countries is dominated almost entirely by small commercial and service enterprises (Rondinelli, 1983). Surveys of four secondary cities and towns in India — Wardha, Ghaziabad, Allahabadk, and Jaipur — ranging from a little more than 80,000 to 1 million in population showed similar characteristics (NIUA, 1987). More than 95 percent of all enterprises in these cities were small or micro (single operator) establishments. From 53 percent of the labor force in Allahabad to 62 percent in Wardha were employed in small informal enterprises. More than half of these enterprises were involved in retail trade or commercial activities. Most of the commercial and retail activities employed the labor of family members and occasionally of one or two hired workers. But manufacturing, services and repair enterprises employed on average from two to five employees and construction enterprises from six to nine paid workers.

Most secondary cities in developing countries have a relatively small share of the country's manufacturing production. In the city of Huancayo in Peru, Long and Roberts (1984) found that about half of the males in the labor force were self-employed or family workers, and 76 percent worked in small informal-sector enterprises. Roberts (1989, p. 41) observed the ease with which people could enter the informal sector; it required "no more than space in a house and a small amount of capital in tools, materials or articles for sale; family relationships provided flexible access to labor, to credit and to economic information."

Although not much attention has been paid to the characteristics of small enterprises in cities of different sizes, some evidence from Kenya suggests that those in large metropolitan areas may differ from those in smaller cities and towns. Hosier's (1987) studies in Nairobi, with a population of more than one million, and in Meru, with fewer than 100,000, indicate that informal enterprises in Nairobi made greater use of nonbinding employment commitments by using a larger portion of casual and family labor than did enterprises in Meru. Small-scale enterprises in Meru did more custom work, had stronger clientele relationships, and tended to earn more income per enterprise than did those in Nairobi. Enterprises could establish closer and more stable clientele networks in smaller towns.

Thus, in both cities and towns, small enterprises and informal-sector activities remain the dominant source of employment. Studies of informal-sector enterprises in Jamaica indicate that they have a remarkable ability to survive precisely because of their small size and flexibility (Doeringer, 1988, p. 467). Small businesses in Jamaica are usually open for customers at all times. They are willing to produce custom goods on order, carry little inventory, have flexible labor practices and can tap the labor of owners and family members quickly. Family members are willing to work long hours and carry few additional costs when they are not working.

Linkages between small enterprises and other segments of the urban economy

Small enterprises play crucial roles in urban economies for reasons other than the labor they absorb. The linkages between informal- and formal-sector businesses in urban areas are quite strong (Rondinelli, 1987). Many of those employed in the formal sector regularly purchase food, goods and services from small enterprises at significantly lower costs, thus raising the real income of many formal-sector workers. Urban street vendors, in turn, purchase a substantial amount of their goods from local wholesalers and producers from nearby rural areas. In Dar es Salaam, Tanzania, for instance, most market and street sellers obtain their supplies from the Kariakoo Market Corporation, the government-controlled national food procurement and wholesaling center. Indeed, the corporation depends on the purchases of these informal-sector participants for a large portion of its sales (Sporrek, 1985).

In the Philippines many of the items sold by "sari-sari" stores — street stalls or small outlets connected to a house — also come from larger groceries and retailers. Barth (1983) found in his studies of the street food sector in Iloilo that about 78 percent of the street vendors sold some manufactured or processed items such as soft drinks, beer, liquor, canned pineapple and packaged snacks originating in Manila; beer and flour from Cebu, and flour and other products from Mindanao. Most of the pastries, breads and baked goods came from local bakeries, and some fresh vegetables and fruits came from commercial warehouses and distributors. Moreover, three-fourths of the vendors use cooking fuels, including wood, charcoal, kerosene, bottled gas, electricity, or some combination of them purchased from retail stores.

Studies of small food enterprises in Santiago, Chile, indicate that the primary source of supplies for nearly half of them is La Vega, the city's largest wholesale food market; about 25 percent obtain their goods from assemblers and wholesalers; 12 percent get most of their products directly from farmers; and about 16 percent obtain their goods primarily from supermarkets or other retail stores (Tokman, 1988). Nearly 78 percent of the sample of small-scale vendors in Jakarta reported obtaining the goods they sold from wholesale outlets and from producers. About 40 percent of the vendors in Semarang and Samarinda reported purchasing goods from retailers (BPPN *et al.*, 1988).

Policies for promoting small-scale enterprises

Despite their critical importance for job creation and economic growth, many enterpreneurs wishing to establish or expand small enterprises in urban centers experience numerous obstacles, including limited access to and the high costs of credit, high hidden costs of start-up and operation, and limited managerial skills. Many lack access to information and technology needed to improve production, efficiency and product quality. They also face difficulties in establishing and maintaining adequate marketing networks, reducing long marketing chains, and responding quickly to changes in market demand. Most smaller businesses cannot compete effectively with larger firms that benefit from preferential government policies and programs (Farbman, 1981; Tendler, 1988).

Experience indicates that the expansion of small businesses depends on increasing the demand for goods and services produced by small enterprises. This requires steady economic growth, and both supply- and demand-oriented policies that promote sustainable economic expansion. In addition, government and private sector procurement programs that seek supplies from small enterprises can help them to increase their production.

Given increasing demand, the ability of small enterprises to expand and create jobs often requires regulatory and administrative changes that allow small enterprise to operate more efficiently; adequate public infrastructure and services; and educational and vocational training programs that improve the quality of the labor force. Improving the efficiency of small enterprises further depends on technical assistance, improvements in management and technology and greater access to credit and materials. (See Figure 1.)

1. *Creating an economic environment conducive*

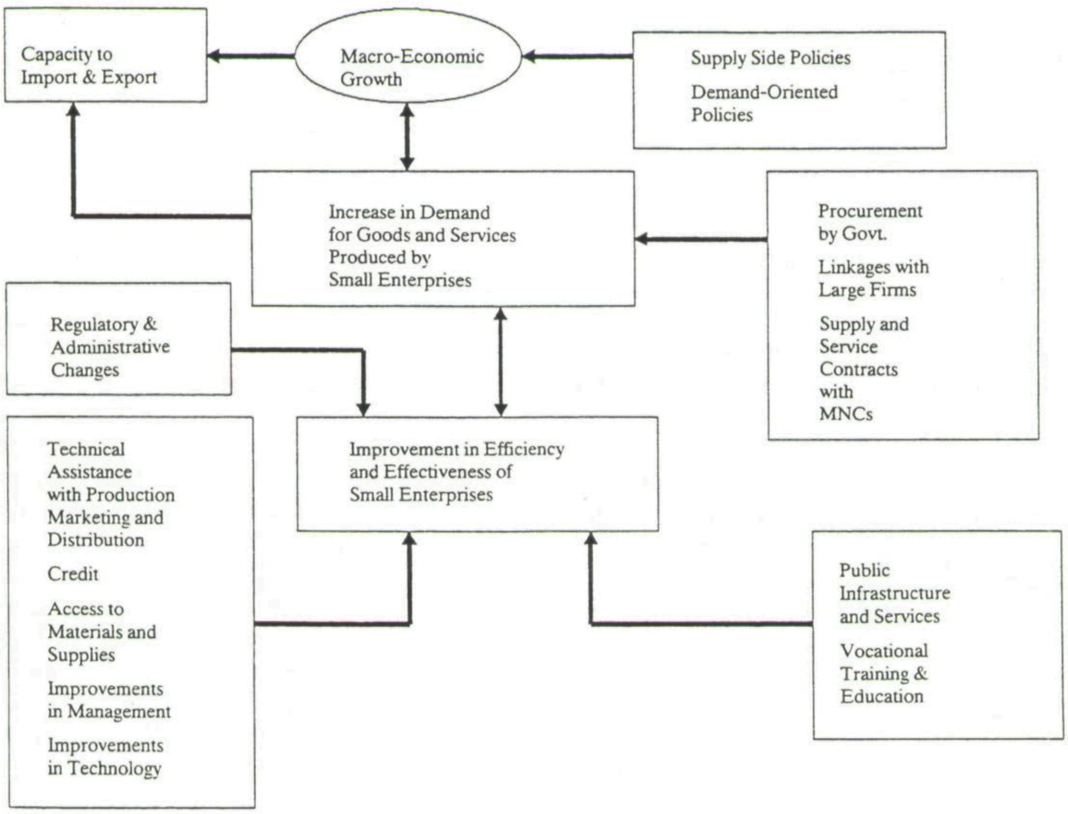

Fig. 1. Factors affecting small enterprise development.

to small enterprise development. The expansion of small enterprises and their ability to generate jobs depends ultimately on national economic growth and on policies that create an environment conducive to private-enterprise development. Governments in developing countries must therefore implement reforms that allow markets to expand and operate more efficiently, including (1) effective fiscal and monetary policies; (2) legislation that offers investment incentives; (3) efficient market mechanisms and competitive practices; (4) appropriate pricing policies for basic commodities and services; (5) incentive-oriented wage policies and merit reward systems; (6) effective policies for establishing foreign exchange rates and allocating foreign exchange; and (7) tax and incentive programs to encourage domestic saving and develop financial markets (United Nations, 1987). Moreover, demand-side policies that increase the purchasing power and income of consumers of informal-sector products, expand subcontracting and piece-rate work between formal- and informal-sector firms, and give small firms equal footing in public procurement, could substantially assist small business development.

The World Bank (1989) points out that supply-side policies are also crucial. Providing credit for operating small and micro-enterprises, training informal-sector owners and workers in better management practices, creating trade organizations and cooperatives to promote the interests of small enterprises both in procuring supplies and in selling their products, developing technologies used by informal sector firms, and improving working conditions for informal-sector participants enhance the prospects for small-enterprise expansion.

Supply-side and demand-oriented policies must complement and reinforce each other. Although perhaps obvious, it is worth noting that public investments in urban infrastructure, public services and human capital (through health and education programs) go a long way in creating conditions that allow small enterprises to operate more efficiently.

2. *Removing regulatory and administrative obstacles to small enterprise development.* In all but a few countries, government policies and regulations are serious obstacles to small enterprise expansion. In Peru, de Soto (1988, p. 23) showed that to register a small garment factory with two sewing machines took five people, including a lawyer, working six hours a day, 289 days to complete the legal requirements. "Ten times they were asked for bribes and were forced to pay them on two occasions in order to proceed." Registering a small transport enterprise in Peru would have taken three years.

In Indonesia, many of those engaged in informal-sector activities try to stabilize their customer relationships and to offer a sufficient variety of goods to attract new customers, but many cannot take the risks involved in expanding their businesses. The most frequently reported problems of Indonesian micro-enterprise owners are difficulties in obtaining permits or licenses to operate in a fixed location, getting access to cheap credit, and obtaining supplies. Street vendors are frequently harassed by local authorities. Most of those engaged in micro-enterprises lack formal training and must learn job skills from other street vendors (BPPN *et al.*, 1987; Demographic Institute, 1989b).

Attempts have been made in many Third World cities to clear vendors from the streets or to confine them to restricted areas. Some municipal governments have passed laws against hawking, imposed high license fees on vendors, and enacted sanitary standards for food preparation that vendors and hawkers could not possibly meet. Street vendors are often subjected to harassment by police or local government officials who solicit bribes to allow them to operate (McGee and Yeung, 1977).

Harassment or restriction has not, of course, reduced or eliminated informal enterprises. Governments in developing countries must take a more positive and active role in encouraging the expansion of small-scale enterprise and informal sectors by perceiving and treating them as entrepreneurs and valuable contributors to the economy. It can reduce permit costs and licensing barriers, allowing them to operate legally throughout the city except in situations where they truly threaten public health or safety. Governments can also provide credit, relax regulations against employing children in stalls and shops, offer basic management assistance, and strengthen the marketing chains of which many small enterpreneurs and informal-sector operators are a part.

3. *Revising and tailoring small enterprise promotion programs to local conditions and needs.* Governments and international development agencies are recognizing the importance of small enterprises to job creation and wealth generation and seeking to develop programs that will strengthen and expand these businesses. But experience suggests that assistance programs to small enterprises in urban areas have had mixed results because they have often been poorly designed and ineffectively implemented (Liedholm and Mead, 1986; Tendler, 1988). Lessons from successful programs can, however, provide guidelines for formulating public- and private-sector policies and managing small-enterprise promotion progams more effectively.

Ashe's (1985) review of micro-enterprise development projects supported by the U.S. Agency for International Development found that successful programs had a number of common characteristics. Most had the strong leadership of a project director who was committed to helping small-scale entrepreneurs increase their incomes. They had concerned and dedicated staff who were interested in the success of their clients' businesses. Program managers and staff had a developmental philosophy that respected the clients' plans, knowledge and ideas and that sought to facilitate them. Good programs usually had community-based selection processes that drew on local people's knowledge of the applicants' reliability and character. They reached a reasonable number of clients without creating exhaustive and cumbersome procedures. Managers of these programs avoided paternalism and excessive formality and kept their procedures flexible. They were willing to change to meet clients' needs as they discovered them. In nearly all of these programs, the managers were concerned about keeping transaction costs low.

For small-enterprise development programs to succeed in creating sufficient numbers of jobs in urban areas, however, studies are needed of their operation and of their growth potential. Special attention must be given to production or processing enterprises that have the potential to employ workers other than the owner and family members. World Bank-assisted loan programs for these small enterprises — in food, beverage and tobacco processing, wood products, metal products, machinery, equipment, and other intermediate and consumer goods industries — have helped create nearly 297,000 jobs during the past two decades (Webster, 1989). The more successful programs were sector-specific, were based on sound analyses of job-creation potential, and focused on helping enterprises with labor-intensive production processes.

4. *Providing capital and credit for small enterprise start-up and expansion.* Although the capital costs of starting and operating a small-scale enterprise are relatively low in most Third World cities, entrepreneurs have great difficulty obtaining loans from financial institutions. Most must rely on personal savings, loans from family or friends, or credit from private moneylenders at high interest rates. About 42 percent of the street vendors surveyed in Iloilo City in the Philippines, for example, borrowed from moneylenders to start their enterprise and paid from 5 percent to 40 percent a month in interest. Most loans had to be repaid within a month (Barth, 1983).

Surveys in Colombian cities likewise found that the lack of financial resources was the primary problem for 68 percent of those enterprises employing less than five workers (Uribe-Echevarria and Forero, 1985). For 20 percent of the firms, it was a secondary problem, but still an important one. Lack of access to financial resources was a major problem for 53 percent of the enterprises with 5 to 10 workers, and a secondary problem for nearly 19 percent. Lack of adequate financial resources was by far the most serious problem reported by all of these small enterprises. The other problems were in obtaining adequate supplies of raw materials, excessive competition from other small-scale enterprises, and personnel management.

Cheap and reliable credit is essential for entrepreneurs to expand. Where governments and the private sector have provided loans to micro-entrepreneurs, they have been used to pay off moneylenders charging high rates of interest, reduce the time-consuming trips to purchase small amounts of raw materials or supplies, reach new markets, improve service quality, and start additional businesses (Ashe, 1981).

But given the limited success of subsidized credit programs in reaching small-enterprise operators who want to expand, governments must reassess this form of assistance and explore alternatives. Options include expanding the numbers and quality of banks, financial cooperatives, and other private lending institutions, and helping commercial financial institutions to meet the credit needs of small enterprises.

Experience in developing countries suggests that credit programs for small enterprises tend to be more successful when they are responsive to both clients' and lenders' objectives; when beneficiaries are selected on the basis of realistic assessments of the enterprises' viability; and when loan criteria ensure access to credit by women and business operators with little formal collateral. Credit programs are more successful when loans are made at market interest rates, dispersed initially in small amounts for working capital, and increased incrementally based on the borrowers' records of repayment (Blaney and Otero, 1985).

5. *Involving the private sector in small enterprise promotion.* Even if promotion programs are on target, the expansion of small businesses depends primarily on increasing demand for their goods and services. In a number of developing countries, multinational corporations (MNCs) are playing a more significant role in assisting small enterprises through special programs that give them preference in subcontracting, procurement and distribution. In Asia and Africa, some MNCs are now seeking raw materials, semi-processed goods, components, finished goods, spare parts, and services from small enterprises. In India, a local affiliate of Philips — a Dutch corporation — operates a "Partners in Progress" program through which it obtains supplies from 1,600 small enterprises that employ 60,000 people. The "co-makership" project helps small enterprises to improve product quality, respond more quickly to changes in market demand, make and deliver products more quickly, and lower their production and distribution costs. Siemens also operates a "vendor development program" in India through which it employs engineers to help more than 1,000 small companies with design, production, and quality control in order to supply inputs to the German MNC (Wright, 1990).

Other MNCs are using small businesses to distribute their products through licensing, franchising, distribution and dealership agreements and to provide support to customers. In Malawi, Nigeria, and India, for example, Lever Brothers created distribution networks for small businesses to serve as distributors, thereby contributing to small-enterprise expansion and training entrepreneurs who create jobs.

6. *Providing technical assistance, training and educational programs through public-private partnerships.* The ability of government to train and educate entrepreneurs is limited in most developing countries. Private organizations must help establish training programs for small-enterprise owners and government extension staff involved in assisting entrepreneurs. In Brazil, for example, a private industry organization — the Confedaracao Nacional da Industria (CNI) — has established several programs to assist small- and medium-scale industrial enterprises (Levitsky, 1990). These programs provide management development and training for consultants and advisors who work with small- and medium-sized industries through short courses, seminars and special meetings. They arrange problem-solving workshops with industry representatives of particular sectors in which small enterprises make an important contribution to production. They offer technical advice and information to groups of small enterprises in the same sector and disseminate information on quality control, productivity, technological innovation, and new processes and products. The industry association works closely with federal, state and local government agencies promoting small-scale enterprise.

The limited success of government technical-assistance programs suggests that there are opportunities for improving performance of small enterprises by contracting with private institutions or non-government organizations (NGOs) to provide extension services, run technology and management service centers, and work with cooperatives on improving production and marketing operations. Evaluations of internationally funded assistance programs have found that they were more successful when they provided only a single "missing ingredient" — such as procurement or marketing assistance or common equipment repair and service facilities — to enterprises that could otherwise operate effectively. Successful programs offered assistance that was based on surveys of effective demand and was industry- and task-specific (Kilby, 1979; Liedholm and Meade, 1986).

International donors are helping public and private organizations in developing countries to assess the effectiveness of and to redesign vocational and skill-training programs for urban workers. The Swedish International Development Agency (SIDA), for example, funds a "sister-industry" program in Tanzania and Zambia that helps create and support small industries. In Tanzania, the program created more than 30 small-scale enterprises that directly generated more than 1,000 jobs in six cities between 1976 and 1987. The program arranged for Tanzanian entrepreneurs to be trained in Swedish firms. SIDA funded contracts that allowed small- and medium-sized enterprises in Sweden to provide the training, "hardware" packages including production equipment, and technical assistance to enterprises that located in industrial estates in Tanzanian cities. Not only did the program stimulate the growth of small enterprises and new jobs, but these enterprises eventually transferred know-how and technology to new Tanzanian entrepreneurs, thereby extending the multiplier effects (Carlsson, 1990).

The German Technical Cooperation Agency (GTZ) uses a "twinning" program to link Chambers of Small Businessmen in Germany with Chambers of Commerce in secondary cities in the Philippines. Through this program, German businessmen provide technical assistance and training to help expand Philippine enterprises. GTZ has also arranged for the German Savings Bank Association to help local banks in several developing countries provide credit to small enterprises more effectively (Frenz, 1990).

Public-private partnerships are crucial in most developing countries because general primary and high school curricula do not prepare skilled workers for formal jobs in urban areas or potential entrepreneurs to start new businesses, and government vocational-training programs are not highly valued by business owners. Governments can play a stronger role by offering incentives for employer training, providing pre-employment schooling and training where market signals indicate demand, establishing vocational retraining for the unemployed, and creating or expanding vocational courses for those interested in self-employment (Middleton *et al.*, 1990).

Summary and conclusions

We began by noting that the ability of the United States to balance its trade will depend in part on the success of American companies in penetrating new markets in developing countries. But the capacity of developing countries to consume U.S. exports will require them to expand their internal markets and to sustain economic growth. A critical need will be to create more than 1 billion urban jobs over the next 35 years to absorb projected increases in their labor forces.

To meet this enormous challenge, international assistance organizations, governments, and the private sector must find new ways to spawn and invigorate small enterprises. These enterprises, both in the formal and informal sectors, have been and will continue to be important sources of livelihood for the vast majority of their urban residents. They also strengthen other segments of the economy which influence trade and investment prospects of U.S. companies.

We have identified and discussed six means for improving the chances of small-scale enterprises meeting the challenges posed by massive projected urban labor-force growth. These include (1) creating an economic environment conducive to small-scale enterprise development; (2) removing regulatory and administrative obstacles to small-scale enterprise expansion; (3) revising and tailoring small-enterprise promotion programs to local conditions and needs; (4) providing capital and credit for small-enterprise start-up and expansion; and (5) involving the private sector in small-enterprise development; and (6) providing technical assistance, training and educational programs through public-private partnerships. If implemented in concert, we suggest that these six approaches would go a long way toward enabling small-scale enterprises to expand in productivity and numbers, and thereby markedly enhance the prospects of developing countries meeting their future job-creation needs.

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