

Interventions for employment creation in micro, small and medium-sized enterprises in low- and middle-income countries. A systematic review¹

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Extended Abstract

Scope of the review

Employment creation has become a top priority for governments around the world. Especially in low and middle income countries (LMICs) the question of how best to create jobs for the large number of people expected to enter the labor force over the next years is a major concern. According to the World Bank's World Development Report 2013 on jobs, Sub-Saharan Africa's labor force is growing by about 8 million people every year while South Asia's labor force grows by 1 million people per month. The report estimates that until 2020 an additional 600 million new jobs will have to be created, predominantly in Asia and Sub-Saharan Africa.

Against this background, the question of how and where to create these jobs has received increasing attention. It has been shown that in LMICs, micro, small and medium (MSMEs) enterprises account for most employment. These MSMEs – formal and informal – typically face several constraints simultaneously. One of the most prominent constraints is access to finance in a broader sense, i.e. access to credit, savings instruments and risk management devices. There are also constraints, which directly relate to the business owners' characteristics, such as lacking financial or management skills, but also gender related constraints. In addition to these constraints operating at the business and individual level, the business environment in developing countries may also often not be favorable

¹ The review is currently being registered with the Campbell Collaboration and will be reviewed by their expert panel. It has been commissioned by the KfW, the German Development Bank, and will be finalized by June 2013.

for the development of MSMEs. Institutional constraints such as deficiencies in regulations concerning property registration and deficiencies in the judicial systems or the registration of credit information may hinder the development of MSMEs. Finally, also related to the business environment, the lack of infrastructure and insufficient quality of public services in terms of water, electricity and telecommunication may further hinder MSMEs. Obviously the different constraints do not act in isolation from each other but rather interact.

Governments, international organizations and other donors have designated substantial resources to the support for the development of MSMEs in developing countries. Notwithstanding these efforts, research on the effectiveness of these interventions in LMICs, and especially as regards employment creation is still limited. Only recently, a number of rigorous impact evaluations have been conducted to assess the impact of various MSME promotion programs. The findings gained by these rigorous and mostly experimental studies provide important insights into the effectiveness of such interventions in promoting the development of MSMEs. However, a common criticism of these impact evaluations – often conducted as randomized control trials (RCTs) – is their limited external validity, i.e. the fact that their findings are not necessarily generalizable. By reviewing the results of a number of impact evaluations from many different sources and contexts, systematic literature reviews provide a tool to test the generalizability of the individual findings.² We hence set out to answer the question which interventions create employment in MSMEs in LMICs through a systematic review of the existing literature on the effectiveness of interventions aimed at creating jobs in MSMEs in LMICs.

Method

The review will follow international standards of systematic reviews in international development, employing a transparent decision making process for literature searching, data collection, quality appraisal and synthesis, drawing on published and unpublished literature to answer the research question and using appropriate methods to critically appraise the literature. Considered studies must in a credible way be able to establish a causal relationship between a policy intervention or a certain set of conditions and job creation. The review will be theory based, i.e. it will be explicitly considered how outcomes may vary by context and the underlying causal mechanisms at work.

Interventions considered

As there are potentially many different constraints faced by MSMEs in LMICs, interventions to remove these constraints, with the objective of creating employment, can take many different forms. In this review, we will focus on interventions that are targeted at MSMEs, but not necessarily exclusively. Interventions that target the labor force directly will only be considered if they aim at the creation of new firms.

Relevant interventions can be grouped into the following broad categories of interventions:

- **Training**

Includes technical and vocational training (in-class and workplace), business skills training, financial literacy training and lifeskills training

² See Petticrew, M. and H. Roberts (2008): 'Systematic Reviews in the Social Sciences, A Practical Guide', Oxford: Blackwell Publishing.

- **Access to finance**

Includes (micro-) credit, grants (cash and in-kind), savings products, (micro-) insurance, guarantee funds and leasing products as well as the establishment of credit registries and credit bureaus, and property rights regulations

- **Business development services**

Include consulting services, management and quality control practices, technology upgrading, market development, export promotion, information provision and networking

- **Research and development (R&D)**

Include the promotion of investments in R&D and of development and introduction of new products and production processes

- **Private sector incentive schemes**

Include wage subsidies.

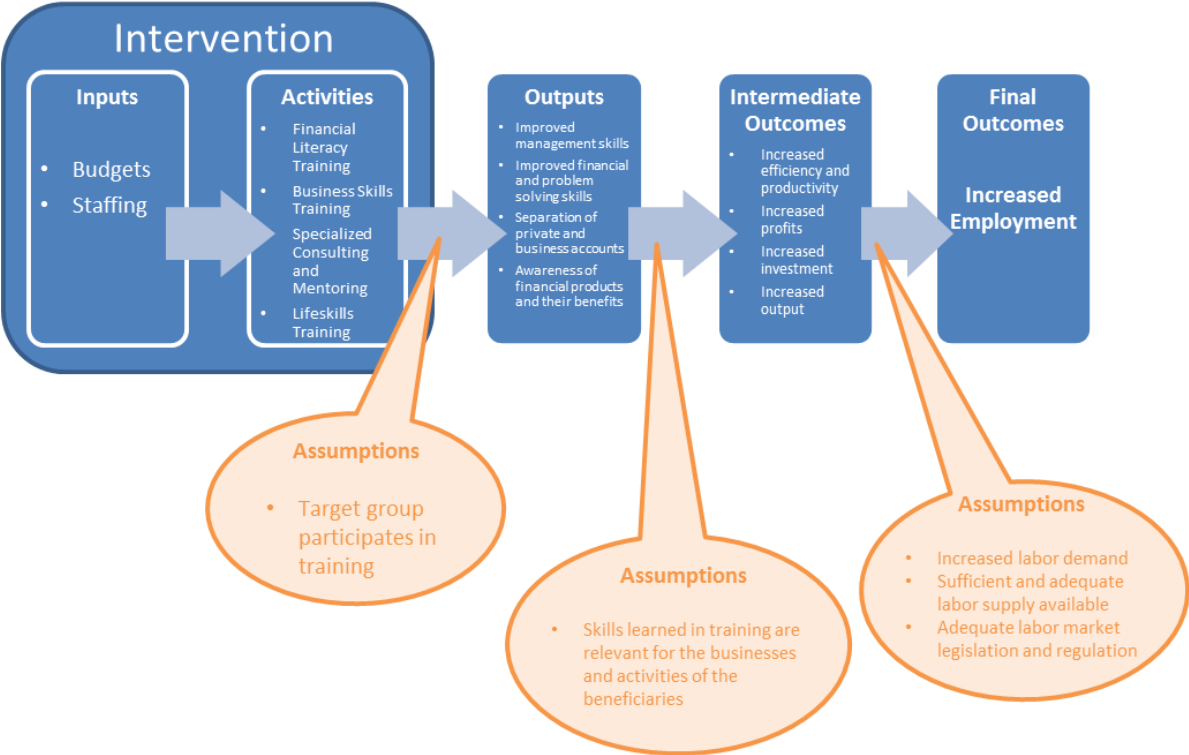
In addition, interventions that can be subsumed under the key word of '*enabling the business environment*' will be considered specifically, if they cannot be classified into one of the categories above.

The interventions considered in this review may in some cases target specific groups, such as the youth, women, the disabled or a particular ethnic group for instance. Furthermore, there might be instances in which some of these interventions are combined and implemented jointly.

Since the aim of this systematic review is to provide a theory-based approach to the question of which interventions create jobs in MSMEs in developing countries, theoretical considerations will help to answer the question of how these various interventions are supposed to unfold their effects in principle. We will present the theory in form of causal chains linking the interventions to final outcomes and then review the results for each intervention along these chains (see Annex). This procedure will also allow to provide a clear mapping of filled and unfilled knowledge gaps in the literature, i.e. for which elements of the chain rigorous evidence exists and for which not.

ANNEX: Causal chains for interventions examined in the systematic review

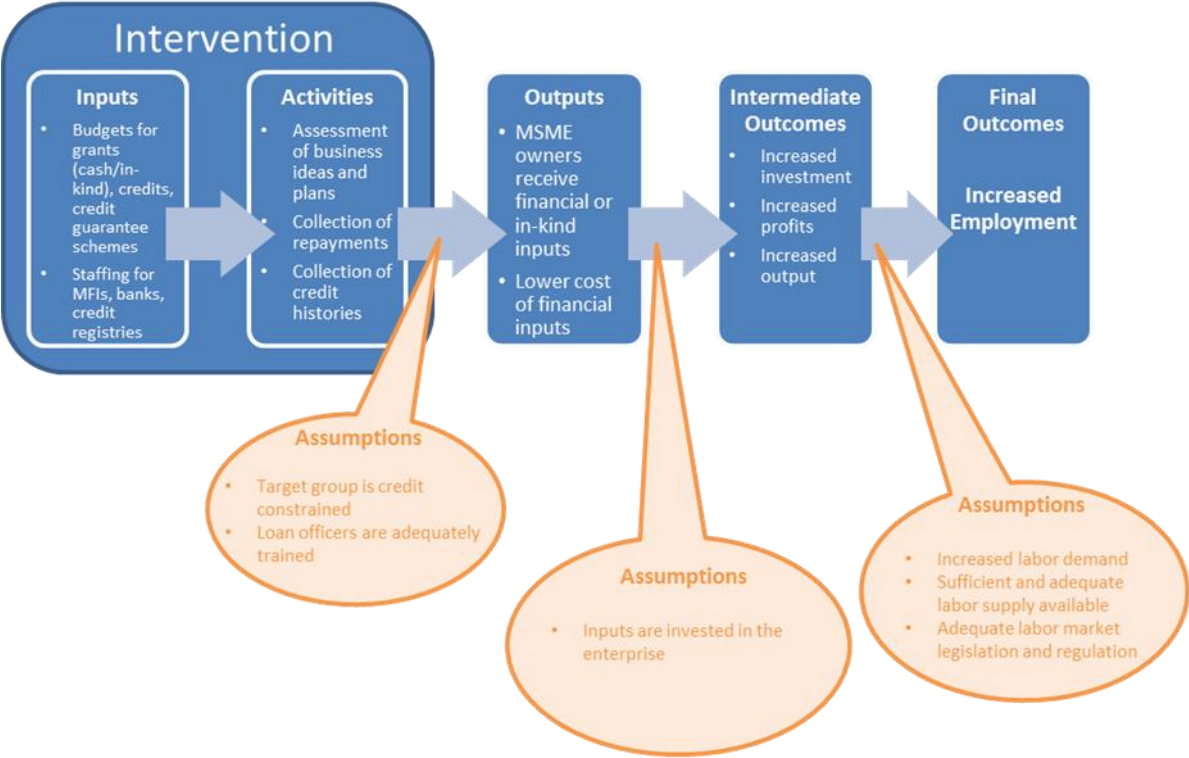
Figure 1: Results Chain for Training



Training

Training interventions might consist of business skills training, financial literacy training, as well as specialized business and management consulting provided to either established MSMEs or individuals who are expected to set up new businesses as a result of the training. Conditional on the assumption that the target group participates in the training and makes use of the consulting services, the intervention improves the management skills of future and existing MSME owners, increases their financial and problem solving skills and raises their awareness of financial products and their benefits for instance. If the beneficiaries of the intervention consequently use these outcomes and apply them to their businesses – assuming that these outcomes are indeed applicable to their contexts – existing MSME owners will be able to increase the productivity of their businesses. Profits will rise due to this productivity increase. If – as assumed by Bruhn et al. (2010) – managerial capital affects the marginal productivity of other inputs, such as labor, profit maximizing individuals will increase their investment in the enterprise and demand more inputs in order to expand production and realize the additional potential profits. As a result, employment in trained MSMEs will increase. This development will of course depend on further factors such as the labor intensity of products and services offered by the MSMEs, the availability of adequate workers and labor market legislation and regulations.

Figure 2: Results Chain for Access to Finance



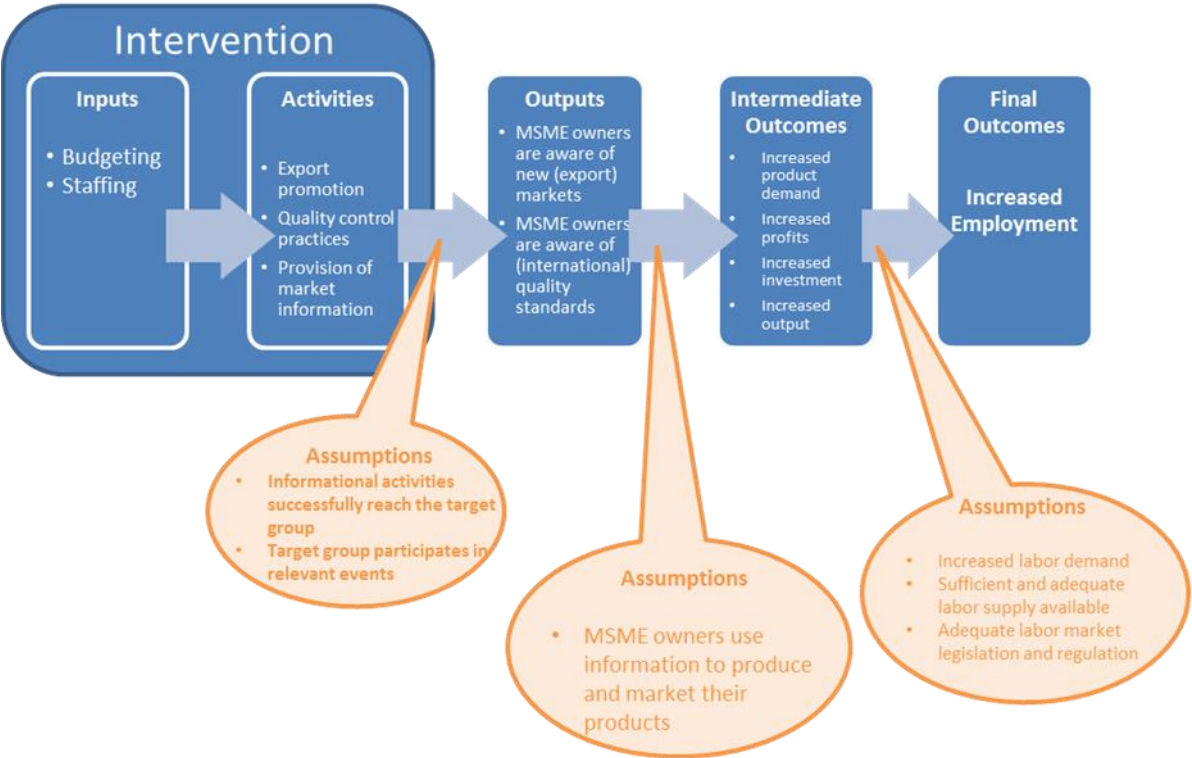
Access to finance

Interventions to increase access to finance may focus on the provision of financial inputs such as cash or in-kind grants, loans, credit guarantee schemes or the establishment of a credit registry for instance. In addition to the financial inputs necessary for implementation, these interventions may require staffing of microfinance institutions (MFIs) or banks. Loans are disbursed to MSME owners or start-ups after a thorough assessment of business plans and ideas, as well as their credit history and collateral. Provided that the target group is credit constrained, these interventions provide them with access to needed financial inputs and/or lower the costs of these inputs, resulting in increased profits. Investment into the business increases output and profits. The expansion of output increases labor demand so that as a final outcome employment in MSMEs rises. Again, the realization of the final outcome according to this causal chain depends on a number of outside conditions and influences that are set out as assumptions in figure 2.

Business development services

Interventions that fall into the group of business development or support services may consist of export promotion programs, the dissemination of quality control practices or the provision of relevant market information to MSMEs. Provided that these activities successfully reach the target group, they raise awareness of new markets as well as processes and measures to market their products more successfully. As a consequence, MSME owners will face increased product demand if they are able to make use of these outputs and can thereby increase their profits by expanding production which again leads to increased labor demand and increases in employment in MSMEs.

Figure 3: Results Chain for Business Development Services



Research and Development (R&D)

The idea of interventions to promote research and development in MSMEs is that the provision of incentives such as tax reductions or subsidized credit increases investment in R&D and leads to increased product development as well as the development of new production processes, marketing and sales strategies. These improvements increase efficiency of the business, which leads to increased profits and output, necessitating an increase in the workforce.

Private sector incentive schemes – Wage subsidies

A common form of a private sector incentive scheme is the provision of a wage subsidy to MSMEs. If MSMEs are willing to hire workers under a subsidized wage, they can realize profit increases and discover whether the marginal revenue of labor is higher than the prevailing wage rate. In that case, after the subsidy expires, MSMEs will retain those workers hired under the subsidization scheme so that the intervention leads to increased employment in MSMEs. This is also the case if the subsidization period allows for productivity increases through on-the-job training of the workers hired under this scheme. After this period, labor productivity will be higher, leading to increased profits and an expansion of production until the marginal revenue of labor equals the prevailing wage rate, again resulting in increased employment in MSMEs.

Figure 4: Results Chain Research and Development (R&D)

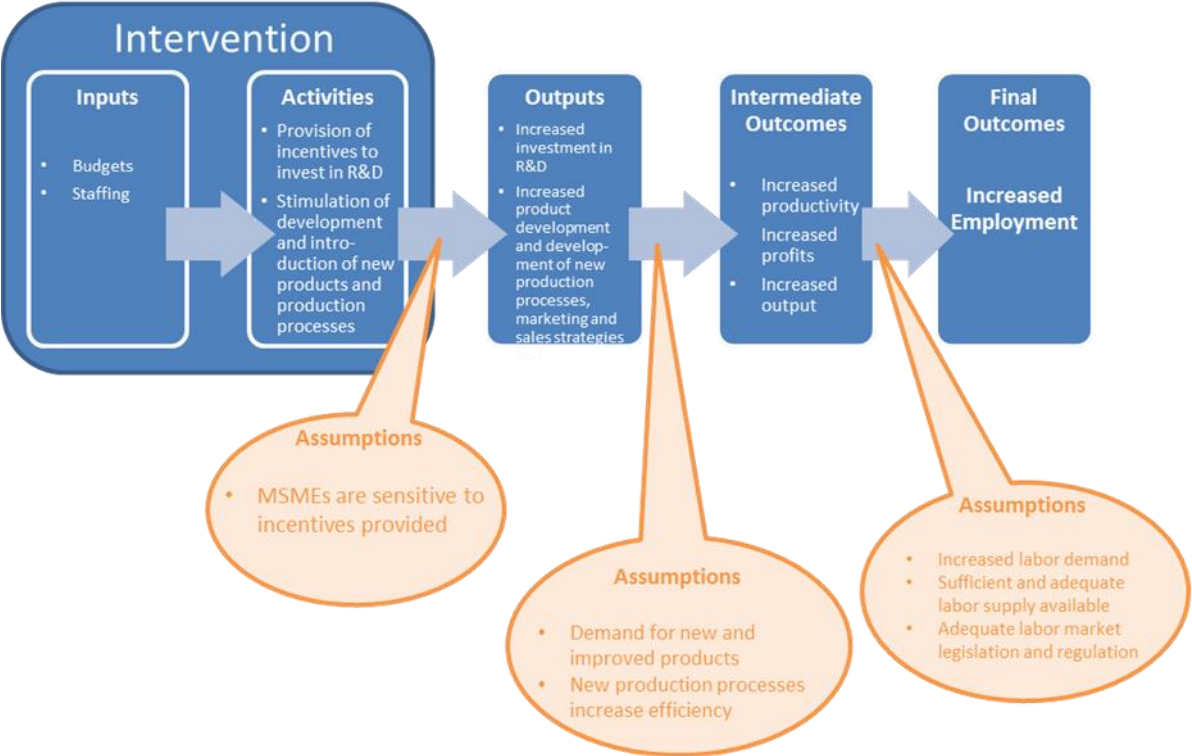


Figure 5: Results Chain Private Sector Incentive Schemes – Wage Subsidy

