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African business systems in a globalising world

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ABSTRACT

The failure of structural adjustment programmes to promote industrialisation in Africa may be at least partly explained by the fragmentation of African business systems. In Africa, the parastatal, foreign-dominated formal and indigenous informal sectors are poorly integrated, largely as a result of the institutional environment in which they have developed. The lack of supportive financial, state and social institutions inhibits trust and accountability, and impedes the access to capital, labour market flexibility, and sub-contracting, which are needed for modern industrial development. More research is needed, both detailed studies of business systems in individual African countries, and cross-country comparisons of the linkages between the economy and the wider social and institutional environment.

INTRODUCTION[1]

In many African countries, industrialisation is seen as a key to development. Manufactured goods offer higher unit values and less volatile prices than either food or cash crops, and industrial jobs promise higher family incomes and improved quality of life, especially for the growing numbers of workers who have little land. Structural adjustment programmes have emphasised measures such as market liberalisation and export promotion, which aim to increase productivity and strengthen the industrialisation process. Yet despite widespread application of these programmes, industrialisation has not taken off as expected in most African countries, and the reasons for its failure are not well understood.

Earlier discussions of this problem have tended to assume that both the industrialisation process and the resulting systems of firms and their interactions would be everywhere the same. Recent studies of business systems in Asia and Europe make it evident that this is not the case. Rather, different kinds of business environments appear to generate very different forms of business organisation (Whitley 1992; Whitley & Kristensen 1996; Evans 1995). The key to understanding how this

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occurs appears to lie in the variety of economic, political and sociocultural institutions that influence the way firms operate.

The comparative analysis of national systems is an important starting point, but it runs the risk of overemphasising their internal consistency, whereas the dominant feature of African systems appears to be precisely their fragmentation or lack of coherence. This article examines Africa's fragmented systems, focusing particularly on the institutions that evolved or failed to evolve. The article argues that the fragmentation of the systems has contributed to the failure of structural adjustment programmes to achieve their desired ends. The analysis focuses especially on eastern and southern Africa, but also draws on material from other parts of the continent.

This article is organised into five parts. It first provides a brief introduction to the business systems perspective. It then describes the main features of the fragmented systems common in Africa, followed by a description of the institutional environment. It next discusses the relationship between the business systems and structural adjustment programmes, and finally draws some preliminary conclusions on why structural adjustment programmes in general do not seem to have had the outcome hoped for, and it underscores the need for further research.

BUSINESS SYSTEMS: THE THEORY

Underlying the notion of a business system is the recognition that business activity does not happen in a vacuum. Rather, businesses are formed and operate in a specific environment. That this environment is peopled by a wide variety of institutions is now widely accepted. Scholars differ, however, on the question of which institutions to include in their analyses.

In the neo-liberal analysis, only the market and government are really important. Other environmental factors are either assumed away or presumed to be the same for all firms. Without denying the actual or potential impact of institutions, neo-classical economists have sacrificed them on the altar of analytic simplicity. Similarly the industrial organisation model that has grown out of neo-classical economics explains the performance of firms and the structure of industries mainly in terms of the size and structure of their supply and product markets (Mason 1939; Scherer 1980). Technology enters the analysis to determine economies of scale, and government policy to change market relations, but these are considered to be essentially external forces.

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What has come to be called the New Institutional Economics (NIE) offers an important corrective to the neo-classical approach. United by a common emphasis on the centrality of institutions to the way business is organised and conducted, the NIE is actually a collection of perspectives, each with its own emphases and definitions (Nabli & Nugent 1989). Williamson (1975, 1985) and North (1986, 1990), for example, focus mainly on economic and political institutions, while Granovetter (1985, 1992, 1995) highlights social and cultural institutions.

The institutions themselves have been variously defined. Nabli & Nugent (1989: 1335) offer a useful working definition: an institution is a set of constraints that governs the behavioural relations among individuals and groups. North (1990) puts it even more succinctly: institutions are *the rules of the game* in a society. Institutions, according to North, include any form of constraint that human beings devise to shape human interaction. These include formal rules and informal codes of behaviour, norms that have been consciously created and those that have simply evolved over time.

The growing literature on business systems attempts to explain the organisation and functioning of industry, using the broad theoretical framework of the NIE (see, e.g. Whitley 1992; Whitley & Kristensen 1996). In a sense, the business system approach does for the NIE what older industrial organisation models did for neo-classical economics. It attempts to examine the forces that direct and influence the way individual businesses operate and, ultimately, the organisation of business activity in general.

The experiences of South East Asia suggest that the development processes are much less uniform than traditional development theory would want us to believe. Studies of the NIC countries show that their development patterns vary considerably (see e.g. Whitley 1992), and recent studies of industrial structures, management practices and work organisation in European countries indicate that here also differences among countries are much larger than traditionally assumed (see, e.g. Whitley & Kristensen 1996). The new theories of national business systems see these differences as a result of variations in the historical development of their institutional environment. Important elements in this institutional environment are, for instance:

(a) financial institutions, both formal and informal, which determine who gets access to credit and capital, and how and to whom

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enterprise management becomes financially accountable (see e.g. Lane 1996);

(b) social structures, processes of socialisation and educational systems, which lead to differences in management practices, trust relations and social responsibilities, hierarchies and delegation in the enterprises and labour market organisation (see e.g. Kristensen *et al.* 1996);

(c) market structures, infrastructures and services, and the legal system and its enforcement, which influence contract and trust relations, collaboration and interaction among enterprises, and possibilities for externalisation and internalisation of activities in the individual enterprise (see e.g. Masinde 1996; Biggs *et al.* 1996); and

(d) technological capabilities and innovation systems, both within individual enterprises and in their environment, which lead to differences in the way management reacts to changes in the environment (see e.g. Bell & Pavitt 1993).

The picture that emerges thus far is of fairly coherent national systems, which differ from one another in important respects. Thus, according to Whitley (1992), Japan, Korea, Taiwan and Hong Kong all have recognisable national systems that are the product of their differing histories and institutional environments. Fukuyama (1995) makes a similar point regarding the Japanese and Chinese systems: history and institutions, especially the nature of the family, have combined to create two distinct patterns of business organisation. In Africa, history and the institutional environment have contributed to the fragmentation that seems to characterise many national systems.

THE FRAGMENTED AFRICAN BUSINESS SYSTEM

During the last 100 years, most African countries have shared a history of colonialism and decolonisation. Despite important differences in resource endowments, pre-colonial social structures, colonial rulers and settlement patterns, post-independence industrial policies and donor involvement, the business systems of many African countries have developed in remarkably similar ways. The typical African production and distribution system consists of several distinct segments: a parastatal sector; a formal, large-scale private sector typically dominated by multinational affiliates, and so-called 'non-indigenous' enterprises owned by migrant traders or settlers such as Asians in East Africa, whites in Zimbabwe and Lebanese in West Africa; and finally

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an 'informal' sector which is mostly African and small scale, but often contains an important illegal or semi-legal large-scale component. The various fragments interact with each other, but only in limited ways, as we will see in the description of each one.

The parastatal sector

At the time of independence in the 1960s, it was generally agreed by the new states and the donors that as there was only limited indigenous African capital, the state had to play an important role in the industrialisation process. In many countries, parastatals were already important, especially in agricultural trade and processing. Before independence they had served to tax the agricultural production, and in the settler economies to monopolise commercial agriculture in the hands of the white settlers. After independence these agricultural parastatals were mostly continued and expanded but with the new states as beneficiaries. In most countries, new parastatals were also created in other sectors of the economy (e.g. banking, transport, wholesale trade, hotels, mining and key manufacturing sectors such as fertiliser and cement), either through nationalisation of existing enterprises, or through government investments in existing or new industries, often through national industrial development organisations. This took place in all African countries, although the parastatal sector probably expanded most in the declared socialist states. According to World Bank estimates, state-owned enterprises accounted by 1980 for 17 per cent of GDP in Sub-Saharan Africa (van Dijk 1994).

One of the reasons for establishing the parastatal sector was a wish to Africanise or indigenise the economy, and this has generally been successful in the sense that the parastatals are generally managed by Africans. However, this indigenisation of parastatal management has coincided with political appointments of top management which have not been supportive of economic efficiency.[2] The agricultural parastatals, in particular, were often supported by trade and price regulations, which should, on the one hand, guarantee both farmers and food consumers a fair price, and on the other, secure a surplus for the state. The fact that the parastatals were also granted a monopolistic position on the market, however, often led to gross inefficiencies and corrupt practices. Therefore, despite generous donor and state support, the parastatals experienced a severe lack of operational capital which made it impossible for them to deliver the services to farmers that were expected of them, and also led to increasing deficits. Thus instead of

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earning money for the state the parastatals became drags on the economy.

Economic policies and exchange rates associated with import substitution policies have in general resulted in low costs of capital goods and led both to a much more capital intensive production system than the cost of labour would warrant, and often to considerable excess capacity. Heavy donor support to many parastatal enterprises and reliance on technology transfer from the donor countries has further aggravated the problems, and often resulted in very low productivity and capital efficiency. Furthermore, the monopolistic status of most parastatals also means that they are generally not well integrated with private formal or informal enterprises.

The formal private sector

The importance of the formal private sector varies from country to country, depending on post-colonial policies to nationalise or indigenise the national economy. Such policies were often directed towards achieving a greater control of the multinational companies or against non-indigenous entrepreneurs.

The formal private sector in many African countries is dominated by enterprises owned by non-indigenous groups. Some, such as the European settlers, Asians, Lebanese or Greek traders, have roots in the pre-independence period. Others are multinationals, often based in the former colonial power. This sub-system of non-indigenous businesses had even before independence developed into an integrated system comprising trade and services as well as manufacturing industries, and often controlling important parts of the import–export and wholesale trade. Although competition among the non-indigenous businesses, e.g. the Asians in east Africa, is often as fierce as with the African businesses, the sub-system of non-indigenous businesses has in most African countries been seen as closed and relating monopolistically to the other sub-systems. The general impression that these businesses are foreign is exacerbated by the fact that the indigenisation of management and, in some cases, employment, has been limited and mostly confined to the lower echelons.

The multinationals, sometimes in joint venture with the state or large private businesses, have invested in manufacturing as well as in other sectors of the economy. The multinational affiliates have generally imported inputs and services from their corporate head-quarters, rather than buying them from local suppliers. This was partly

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because local supplies often were irregular and of low standard, but, more importantly, because many of the multinationals earned their profits on the imported inputs rather than on the final products. In contrast to the local large-scale businesses, multinational affiliates have often indigenised both management and employment to high degree.

Although the price of imported production inputs and capital goods have generally been kept low by favourable exchange rates, import licences and access to foreign currency have only been accessible through the state. The multinationals have, therefore, like the private sector in general, depended on access to the state, often through some clientelistic relation to the central political and administrative system.

For most commodities, production has been highly concentrated on a few or even a single enterprise, and ownership control has often been even more concentrated (see e.g. Rasmussen 1992). Even where there have been more producers, collusion between them has been common, and where there have been many producers, wholesale trade has often been concentrated. For instance, in Kenya, although African businessmen have increasingly ventured into the wholesale of groceries and other consumer goods since Asian traders were banned from the rural areas and small towns in 1967, important parts of the import–export and wholesale trade seem still to be controlled by a limited number of Asian businessmen. In Zimbabwe and South Africa the dominance of large retail chains, which serve as their own wholesalers, means that the wholesale sector is so underdeveloped that small and medium-sized producers are often forced to retail their own products (Pedersen 1997b).

In the post-independence period most governments have tried to break this monopoly, through industrial and trade policies designed to support the development of indigenously owned enterprises, either parastatal or private. Despite such policies, the development of private indigenous businesses, especially in manufacturing, has been fairly slow in most African countries, and mostly limited to small and medium-sized enterprises. Many countries with declared socialist governments, such as Tanzania, Ethiopia, Mozambique and Zimbabwe, have been reluctant to develop an independent indigenous business class which could compete for political power. In other countries, e.g. Kenya, the rivalry between different indigenous groups has constrained the development.

In East Africa, states have in different ways attempted to break the private wholesale monopolies. In Kenya, the state created its own corporation to engage in wholesale trade in groceries and other

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consumer goods to compete with the private wholesalers, and at the same time limited the activities of the Asian businessmen in the rural areas. In Tanzania, the government created state monopolies, while in Uganda Asian businessmen were expelled. These policies have limited the activities of Asian traders in the rural areas, but not their dominance in the wholesale sector. They also forced some Asians into manufacturing (especially in Kenya), and others to migrate, which in time has helped Asian businessmen to expand their international networks.

The closed and monopolistic position of important parts of the wholesale sector has made it difficult for new African businesses to get into anything other than small-scale production, services and retail trade. On the other hand, the relatively inefficient production and high prices in the formal sector have made it difficult for it to penetrate the low-income markets, and therefore made room for an often large informal sector.

The formal private sector in general, but especially the large indigenous businessmen, have generally been highly dependent on the state (Gibbon 1996). The import substitution policies prevailing in most countries after independence implied a strict regulation of imports and foreign currency that made the private sector no less dependent on the state than the parastatal sector. In many countries the ruling class, or often more specifically the ruling political party, has used state control of scarce resources and licences to control access to the private formal sector. Foreign currency controls, mining rights, land distribution and business licensing were all, in various times and places, means to this end. Therefore, the ruling party in many countries appears to control a large part of the indigenously owned private sector through a system of patron–client relations.

The investment of African businessmen in the formal sector has mostly been in large-scale agriculture, real estate, trade, transport, finance or other services, and only to a limited extent in manufacturing. In a sample of 100 Kenyan manufacturers, Himbara (1994) found that 75 per cent of the enterprises were owned by Kenyan Asians, while only 5 per cent were owned by Africans, 9 per cent were parastatals or publicly held, and 11 per cent were foreign/joint ventures. In addition, the Asian share of new manufacturing establishments had been growing since independence, and amounted to 85 per cent of firms established since 1980.[3]

The reason for this dominance of non-indigenous businesses in manufacturing and wholesale trade is not clear. They may be operating

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on financial and organisational traditions or principles which are more efficient, as Cowen & MacWilliam (1996) claim. Alternatively, they may have developed better international contacts or special political connections; or they may simply, as Himbara (1994: 69–70) argues, have accumulated enough resources from their commercial activities to enable them to take advantage first of colonial efforts to industrialise and later of the post-colonial governments' tolerance of their participation in manufacturing.

The informal sector

Outside the formal private sector, and partly outside state regulation, operates the so-called 'informal' sector. It consists mostly, but not only, of small and micro-enterprises and we shall here mainly be concerned with those. However, the term is very ill-defined: it may contain enterprises carrying out illegal activities like smuggling or drug trade; others which carry out legal activities but which do not pay license or tax as expected and operate on land which is not their own; and still others which operate perfectly legally but below the threshold where they need to register as a company and pay company tax. Small informal enterprises have only rarely had access to formal financial institutions, state resources and state protection. Most African countries have since independence or even before had small enterprise development organisations and policies, but these have generally not had a high priority. Industrial policies have, at least until recently, focused on large-scale production. Small enterprises, often seen as a threat to the monopoly of large formal sector enterprises, have been harassed by state or local authorities (see e.g. Havnevik *et al.* 1985; Sverrisson 1993).

The small informal enterprises are very heterogeneous, consisting of enterprises often operating in market niches not served by the formal sector, and utilising human and financial resources and production inputs not useful or accessible to the formal sector. As a result there is no clear distinction between small formal enterprises and the larger informal enterprises. Therefore we prefer to talk about 'small' instead of 'informal' enterprises.

There are important forward linkages between the large-scale formal producers and informal small-scale traders and retailers who market a large part of the industrial produce and sometimes utilise their by-products. There are, however, few commodities and services going the other way, and sub-contracting relations are infrequent except in

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industries like construction where speciality based subcontracting appears to be fairly common in Kenya and Zimbabwe (Rasmussen 1992; Godana *et al*. 1997; Kinyanjui & Mitullah 1997) though less so in Tanzania (Ærøe 1992).

Mutual collaboration among small enterprises and the development of agglomerations of small production enterprises in industrial districts is also infrequent, although there are examples of this in Ghana, Kenya and South Africa (McCormick 1998). In Zimbabwe, Pedersen (1997b) found examples of informal trade linkages where rural retailers distribute goods produced by family members running small manufacturing businesses in town. Especially, but not only, in West Africa there are also examples of large trader networks, often trading internationally and illegally, but with links to the formal economy (Meagher 1997).

Mobility of labour also tends to be one-directional. Studies show that many small entrepreneurs have been employed in the formal sector before setting up their own enterprises. They have been trained there and saved for the initial capital from their wages. There seem to be fewer people going the other way, although there are few empirical studies of this.

Most small enterprises are started on the basis of their owners' savings. These savings are in many cases from wages earned in the formal sector, but in general the capital flows seem to go the other way: Some of the savings from small entrepreneurs are placed in the banks, which mostly lend money to the formal sector. Small enterprises rarely borrow from banks, partly because they do not have collateral, in the form of title deeds to their land. Therefore, in connection with the structural adjustment reforms, there has been pressure to change the land legislation to provide more widespread titling. Experiences from Zimbabwe (Pedersen 1997b) and Kenya (Tomecko & Aleke-Dondo 1993), however, indicate that title deeds may not be sufficient to secure loans for small enterprises, because it is still uncertain whether it will be politically acceptable for the banks to take over communal land from people who do not service their loans, or possible for them to sell the land on the market.

Therefore enterprises seldom go broke. They may not have sufficient capital to pay their bills and continue operation, but they will continue to own the fixed assets of the enterprise because nobody is interested in taking them over (see e.g. Pedersen 1997c). Often, when enterprises stop operating they are not sold; they just close and are written off. Thus although thorough investigations do not exist, domestic markets

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for second-hand production machinery appear to be little developed. This reduces the possibilities for small enterprises to move upwards, and may be an important reason for the 'missing middle' in the enterprise structure often talked about in the literature (see e.g. Fafchamps 1994; Ferrand 1997).

THE INSTITUTIONAL ENVIRONMENT

From the above discussion, it appears that the different parts of the African business systems have not been well integrated in terms of inter-enterprise trade and production links. Many enterprises are operating in semi-monopolistic markets, vertical specialisation and sub-contracting are infrequent, and both formal and informal private indigenous businesses tend to be kept on the margins of the non-indigenous business sub-system. Large enterprises seem to rely to a large extent on access to state resources. Small ones are left to fend for themselves; when they do interact with government, it is often to buy protection or otherwise cope with the negative impact of government harassment. However, at all levels and segments of the business system there are important financial, political and social links to the institutional environment, and enterprises are often interconnected through these links. The hypothesis advanced here is that the fragmentation of the African business system is a result of the institutional environment in which it has developed. The following section discusses in some detail the institutional environments in which these systems have evolved. The institutional environment is partly a function of the state, but it is also embedded in the broader social institutions and in the business system itself, and it comprises activities and policies at micro-, meso- and macro-levels.

Financial institutions

Before independence, the official banking systems in many African countries were largely reserved for the white owned businesses, while the migrant trader communities to a large extent had developed their own banks and internal financial institutions. African businessmen were excluded from both, and were therefore limited to their own savings, family loans or the informal financial market comprising money lenders, trader credit, savings and credit societies and rotating savings and credit associations (see e.g. Bagachwa 1995; Daniels *et al.* 1995). In order to improve access to the financial markets for African

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entrepreneurs, some African countries, for example Tanzania, nationalised the banks after independence, while others, such as Kenya, Zimbabwe and Nigeria, attempted to set up new indigenous banks. Both strategies have met with limited success: the first, because state capital in too many cases was allocated on political rather than economic criteria; the second, because many of the new banks were merchant banks based on foreign currency speculation rather than savings capital. They were established in order to secure cheap loans for their owners, and therefore soon went bankrupt, apparently in many cases because the owners had emptied them of capital (see e.g. Lewis 1994 on Nigeria; and *The Daily Nation*, Nairobi, 5–6.11.1996 for a Kenyan case). As a result the financial markets have stayed fragmented. In Kenya, for instance, the Asian businesses have to a large extent relied on mutual financing, the multinational affiliates on foreign capital, the parastatal and a few large African owned private firms on state capital, and the small African businesses on their own limited savings and informal or NGO credit. Personal savings accounts for the largest share of small enterprise capital, partly because of the scarcity of alternatives, and partly because there is often no other place to invest limited private savings than in a small enterprise (Fafchamps 1994).

Social structures and labour market organisation

Management practices and organisational structures in African countries are generally very hierarchical, and delegation of authority is limited (Dia 1996; Kuada 1994). There are deep-rooted historical and social reasons for this. Many parts of Africa have inherited patriarchal social and family structures from the pre-colonial period. At the time of colonisation European organisational and social structures were very hierarchical. In the colonies the hierarchies became even steeper, both for racial reasons and because the skill levels were lower than in Europe. However, steep hierarchies and low skill levels tend to be self-reinforcing, because with steep hierarchies and little delegation, there is no reason to raise the skill level, and with low skill levels it is difficult to delegate.

Improved education became one of the most important post-independence goals of many of the new states. But education meant academic education and training for management jobs, not artisanal or technical training. Therefore, although the Africanisation of the civil service as well as the management of parastatals and multinationals has been fairly rapid in most countries, the organisational structures in

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industry have remained hierarchical and based primarily on unskilled labour. This has undoubtedly been a major hindrance to productivity increases within the enterprises, and also to the possibility of externalising tasks to sub-contractors and service firms. On the other hand, the growing level of education, together with the slow growth in formal employment, means that the level of education among small entrepreneurs has increased rapidly during recent years, and led to the establishment of new types of activities in the informal sector (see e.g. Pedersen 1997c).

Infrastructure, market structures and the development of trust

One of the prerequisites for the highly integrated and globalising production systems in the industrialised and industrialising countries has been the development of a dense network of infrastructure and business-related services, which have played a major role in increasing production and distribution efficiency, and in developing and maintaining international markets. In Africa this only exists to a very limited extent today. In many countries the existing infrastructure is overloaded and in bad repair, and services are unreliable and often expensive and infiltrated with corruption. Wholesalers and trading agents, who in other parts of the world play an important role not only in the distribution of consumer goods but also in the development of inter-enterprise trade and the spread of market information and product innovations to the small enterprises, are little developed and often monopolistic.

In Kenya, for instance, Asians control most of the wholesale sector, and in Zimbabwe the dominance of large retail chains operating as their own wholesalers means that an open wholesale sector has failed to emerge. As a result, small and medium-sized producers are forced to develop their own distribution system if they want to expand beyond a very local market. Some travel themselves, using the public transport system, while others entrust their goods to mobile traders. In many African countries, monopolistic or illicit tendering practices and the inability of the legal system to secure enforcement of contracts is a major problem, especially for small and medium-sized enterprises (Fafchamps 1996; Kimuyu 1997). Therefore they need to base their business relations on mutual personal trust. However, even personal trust depends on the availability of social and state institutions, infrastructures and services. Trust in a businessman (or woman) is often interpreted to mean trust that he will not cheat or act

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opportunistically. However, trust is broader than that. With reference to Sako (1992), Humphrey & Schmitz (1996) distinguish between three different elements of trust:

(a) contractual trust, that the businessman will act honourably;
(b) competence trust, that the businessman has sufficient technical and organisational capacity and capital or credit-worthiness to fulfil his obligations; and
(c) goodwill trust, defined as mutual expectations of open commitment to each other. Goodwill trust is the basis for long-run collaboration.

Contractual trust may initially be ascribed to family members, or people from the same ethnic group with whom the business person has mutual social obligations. But business trust is gradually expanded over time as a result of the experience of continuously testing the trust. In a study of grain traders in Uganda, Sørensen (1997) describes how this process of testing and extending the trust takes place often over a period of many years. However, in unstable and risky environments, such as Africa, competence trust may be as important as contractual trust. It does not help a poor, small-scale businessman that he is trusted to be honourable, if there is a large risk that he will be hit by events beyond his control, such as robbery, illness or drought, which may prevent him from fulfilling his contractual obligations.

The more unstable and risky the environment, the more difficult it is to be trustworthy. In industrialised countries, insurance, social security systems, efficient law enforcement and access to public and private infrastructure and services all tend to reduce the individual competence necessary to become trustworthy. In African countries such public services, if available at all, are often accessible only to the large enterprises. The fact that these mostly exclude small enterprises may be one very important reason why it is so difficult to bridge the gap between small and large enterprises. The deficient institutional environment leads large enterprises to develop their own infrastructure and services, either in-house or in collaboration with selected other enterprises. This results in the development of closed circles of trust, which further fragments the business system.

Technological capability and innovation systems

To an increasing extent, the present process of globalisation is based on externalisation of activities from the enterprise, and their regrouping on a local, national, regional or global scale. This process of

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externalisation rests on increasing product specification, quality control and standardisation, not of the final product but of components and intermediate inputs which go into the final product. In most African countries few manufactures are able to live up to these requirements and the level of technology has increased only slowly, if at all.

The level of education in most African countries has increased dramatically since independence, but this generally has not led to increasing levels of industrial technology and productivity. A three-country World Bank sponsored study, including Kenya, Zimbabwe and Ghana, found that multinational and local expatriate-run firms in each country generally have the necessary skills in-house or available through the parent company to acquire technology and execute investment projects efficiently (Biggs *et al*. 1995). A few indigenous large enterprises have similar capabilities, but most firms, large and small, operate at low levels of technology and efficiency. Mwamadzingo (1996) found in a study of technological change in small and medium-sized Kenyan industry that, instead of moving out of simple labour intensive activities, firms are increasingly substituting skilled labour with unskilled.

Although many African countries have set up technological centres to support the process of technical change, their effects have not been impressive. The same World Bank technology study not only found very low levels of technology even in the large enterprises, but also reported that only 10 per cent, 15 per cent, and 26 per cent of the firms in Ghana, Kenya and Zimbabwe respectively had undertaken any systematic research aimed at improving products or processes (Biggs *et al*. 1995). Very few enterprises have special sections for technological development or R&D, and quality control, where it exists, consists mainly of visual inspection of the final product. In industrialised countries, new technologies are often diffused through sub-contracting relationships. Sub-contracts between larger manufacturing firms and small formal or informal businesses are found in Africa, but very seldom lead to technological upgrading of the small enterprises. The very low level of technology in the large enterprises may be the most important reason for this. At present, most technical innovation in African enterprises takes place through the import of new machinery supported by expatriate experts. Learning processes within the enterprises are hindered by hierarchical organisations and low skills, and the very fragmented production and distribution system limits the diffusion of innovations through the enterprise system.

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Social institutions: gender, household, clan and ethnic relations

In most African countries large parts of the population have little or no access to the state's social security and legal systems. Income transfers through informal social institutions and ethnically based patron–client relations serve as safety nets, protecting both small entrepreneurs and employees in larger enterprises against illness, fire, theft, robbery, traffic accidents, bad luck in business, job loss and other unforseen events. Therefore, at the same time as the family is an important source of capital to start a small enterprise, family responsibilities may also tap the enterprise for resources at a later stage, making it difficult to accumulate. Writing on Uganda, Whyte & Whyte (1996) say that success in business is highly respected, but the success is a public good which the businessman or woman must be prepared to share. Therefore a business needs to grow beyond a certain threshold before it can both accumulate and honour its social responsibilities. Informal discussions with African colleagues suggest that attitudes towards business success and the expectations of sharing its rewards with the extended family may vary from one community to another, and that such variations may partly explain why some ethnic groups are better represented in business than others.

The social requirement to transfer of resources requires readily available cash. Based on an investigation in Senegal, Dia (1996) found that members of savings circles have lower transfers than non-members. He also found that people invest in fixed assets and consumer durables in order to reduce their income transfers. This may be one of the reasons for the recurrent cash flow problems which seem to be typical for small African businessmen, and for the tendency to over-invest in fixed assets, like shop buildings and machinery, which end up unused for lack of cash (see e.g. Pedersen 1997b).

The state

Discussions of industrialisation in Africa frequently revolve, implicitly or explicitly, around the state. The lack of a dynamic and efficient industry is attributed to policy failures on the one hand, or to weak or missing national or local-level institutions, on the other. Mkandawira (1998) presents a critical discussion of these different arguments, and concludes that the main problem is that African states have in general been unwilling or unable to develop a capitalist class to carry out development.

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Trade and industrial policies in many African countries have attempted to develop a production and distribution system owned and controlled by Africans, which could supplement or substitute the non-indigenous business systems dominating most countries' economies. These policies have generally not succeeded. One important reason for this is, as Himbara (1994) concludes in his study of Kenya, that the non-indigenous businesses were there first and were already well consolidated at the time of independence. But another reason appears to be that policies to create alternatives to the non-indigenous businesses have not been consistent. The most persistent policy focus has probably been on the parastatals, but they have been perceived as objects of taxation and resources control, rather than as potentially productive enterprises. Policies towards multinational corporations have shifted between support and restriction. Policies towards private indigenous businessmen have been half-hearted because the ruling group has often seen them as potential rivals for power. Furthermore, there is often a serious discontinuity between policy and implementation. For example, Kenyan policies for the small enterprise development have been very supportive on paper, while government harassment, extortion and property destruction continue unabated.

The state is also implicated when fragmentation is explained by weak, malfunctioning, or non-existent political and economic institutions. Institutions, in the Northian sense of 'rules of the game' must develop and change if industrialisation is to proceed (Nabli & Nugent 1989; North 1990). Part of the change is the development of national institutions, which either replace or coexist with the more localised institutions common in agrarian societies. Appropriate political and economic institutions enhance economic growth, while weak or rigid institutions fail to provide the necessary framework for business activity. The lack of a coherent and predictable institutional framework may deter business activity altogether or it may result in fragmentation.

Institutions surrounding property rights, contract enforcement, the organisation of work, the availability of information and collective action are critical determinants of the nature and extent of industrial development (Williamson 1985; Whitley 1992). Studies are just beginning to document the institutional problems in each of these areas. For example, the issue of contract enforcement has been explored in both Kenya and Ghana (Kimuyu 1997; Fafchamps 1996). Findings suggest that the lack of effective institutions to enforce commercial contracts adds to the riskiness of the business environment, and encourages entrepreneurs to restrict their dealings to persons they know

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and trust. This, of course, militates against the building of wider regional or national markets for goods and services.

HOW IS STRUCTURAL ADJUSTMENT CHANGING AFRICAN BUSINESS SYSTEMS?

The original purpose of the structural adjustment programmes, which most African countries have initiated under pressure from the World Bank and the donor community, was to change the institutional environment in support of more productive activities and higher efficiency in the economy.[4] However, this goal has only to a limited extent been fulfilled. The main ingredients of structural adjustment programmes have been:

(a) foreign trade liberalisation and devaluation;
(b) deregulation of the national markets and elimination of consumer subsidies;
(c) reduction of public sector employment and privatisation of parastatal enterprises or at least changing them to operate on market principles;
(d) support for development of the private sector in general and especially the small-scale/informal sector by creating a so-called enabling environment, through provision of credit and training schemes for small entrepreneurs and policies to reduce the legal regulations and administrative practices which until now have hindered its development.

The immediate effect of the deregulation of the national markets and of devaluation has been large price hikes which have resulted in a dramatic reduction in buying power and contractions in the home market in both rural and urban areas. Although the deregulation has generally resulted in higher prices to the farmers, only those, often few, farmers who have a production surplus to sell, benefit from the higher prices. Small farmers who are not self-sufficient in food rather suffer from the increasing prices on food and farm inputs.

Buying power has been further eroded by reductions in formal sector employment, resulting from privatisation and public sector retrenchments, although in most countries both privatisation and public sector retrenchment have been limited and slow to materialise (van Dijk 1994). Even where parastatal organisations have been privatised, they may reappear in new private or semi-private forms, as happened in the shea trade in Ghana (Chalfin 1996). The contraction of the home

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market has also been aggravated by increased import of cheap consumer goods, especially from Asian countries, and second-hand clothes from the United States and Europe. On the other hand, these same cheap goods have made it possible for poor consumers to survive on meagre incomes. Liberalisation has also reduced the cost of some foods. For instance, in Zimbabwe the liberalisation of the grain trade has meant that grain deficit areas which earlier could only buy expensive industrially processed maize can now buy unprocessed maize and have it milled in local hammer mills, and thus save more than 20 per cent of the price of industrial mealy meal (Jayne & Chisvo 1991).

Deregulation and trade liberalisation have also opened up new possibilities on the home and export markets, respectively, albeit to a more limited extent. Different groups of enterprises have responded differently to these new opportunities. Deregulation of domestic agricultural markets has opened new opportunities in both agro-processing and trade, which to a considerable extent seems to be taken up by indigenous businessmen, often former trading agents or employees of the parastatals. The multinational affiliates which earlier only served the protected home market, now attempt to serve a wider African market. However, this means that they no longer need a plant in each country, and may therefore concentrate their facilities in the more industrialised African countries. Thus, for instance, Kenya hopes to become a so-called 'hub' for DFI in East Africa (*The Daily Nation*, Nairobi, 2.11.1996), and Ghana hopes to become a hub for West Africa (Afenyada 1997). The non-indigenous enterprises also increasingly attempt to produce for the export markets both inside and outside Africa. In general, however, considerable changes will be necessary if manufacturing industries are to become competitive in export markets, and with imports in the home market. Investment has therefore tended to shift from manufacturing, either into imports or into real estate, non-traditional export crops (e.g. vegetables and flowers), mining and fisheries (Gibbon 1996).

To gain access to export markets, a number of African countries have established export processing zones or programmes for export processing under bond, modelled after the success of some of the low-income Asian countries and Mauritius. Thus from 1990 to 1994 Kenya licensed fifty-five garment export firms to produce under bond. By December 1994 these firms employed nearly 15,000 workers.[5] Some are run by Kenyan Asians, but many appear to be firms based in Southeast Asia, engaged in so-called triangular trade in order to by-pass export quotas put on their home countries. These enterprises in Kenya were

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apparently price-competitive with producers in the Asian countries (Biggs *et al.* 1996). When the USA in 1994 imposed a quota on imports of Kenyan pillow cases and boys' shirts, many firms closed down and others cut employment drastically. By early 1996, employment in these exporting firms had dropped to only 3,300 (*The Economic Review*, 11–17.11.1996).

Small formal or informal African enterprises have probably been hit hardest by the contracting home market. Their small size and lack of international contacts make it more difficult for them than for the non-indigenous enterprises to break into the export market. On the other hand, many donors and NGOs have established credit, training and other support programmes for small and medium-sized enterprises, hoping to expand employment and be able to fill out 'the missing middle' in the hierarchy of enterprises. Donors have attempted to engage the commercial banks in the administration of these programmes, and many banks have established their own small enterprise programmes. Some donors have also established so-called enterprise-to-enterprise support programmes, which attempt to link African enterprises with enterprises in the donor country on a near-commercial basis (in contrast to the old sister-industry programmes which were heavily subsidised). Such efforts, however, have in general been very slow to develop and have reached only a few enterprises.

To increase the competitiveness of small and medium-sized indigenous enterprises, the government of Zimbabwe has established a policy of 'affirmative action' which prioritises indigenous businesses on public tenders below a certain size, and requires large white-owned enterprises winning larger tenders to subcontract part of the contract sum to indigenous businesses. Similar policies have been discussed in South Africa.

Donors have also attempted to support the development of subcontracting relations between small and large production enterprises, but this has generally been much less successful than in Asian countries. Where such relations have been established, only very simple operations have been subcontracted, and there has generally not been any attempt by the large enterprise to up-grade the technology of their subcontractors. Even in South Africa, where the level of technology is somewhat higher, subcontracting in the garment industry, for example, consists mainly of cut-make-and-trim operations (October 1996). One of the reasons for this is probably the low level of education in South Africa during the apartheid regime (Rogerson 1998).

Wholesalers and trading agents, which in Asian countries have

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played an important role in channelling technical and market information back to their suppliers (see e.g. Weijland 1994), also appear to play a more limited role in Africa. South Africa, at least in the clothing industry, may be an exception. South Africa's clothing industry is mainly oriented towards the domestic market, where the large national retail chains play a key role in design and fabric selection. In the growing, but much smaller, export market, agents are beginning to play an important role in transferring information and design techniques, and in ensuring quality standards (October 1996).

Implementation of attempts to change the policy environment in favour of small enterprises have in general been slow. In most African countries, they appear to be met with reluctance and conflicting interests. Licensing and regulation requirements are sources of revenue for central and local governments, and of rents for officials. In many countries lack of law enforcement appears to be one of the worst hindrances for development of private businesses. This makes it impossible, especially for small businesses, to take legal action in cases of breach of contract or theft or to obtain protection from harassing officials (see e.g. Sørensen 1997).

Thus, although the small-enterprise sector is mushrooming, the major part of it has maintained its pre-SAP character. There are signs of increasing diversification (see e.g. Müller 1996), and the development of more mechanised enterprises in, for instance, milling in Zimbabwe and Uganda (Pedersen 1997a), furniture production in Kenya and Zimbabwe (Sverrisson 1993) and machinery manufacture in Kenya (King 1996). The small-enterprise sector also appears increasingly to engage in its own small-scale trade with neighbouring countries independent of the formal sector. On the whole, however, small-scale manufacturing continues to use low-level technology to produce cheap consumer goods that are competitive only on the home market.

It appears, therefore, that structural adjustment has not achieved its twin aims of increasing both production and efficiency. Domestic markets, although deregulated, remain small, and few countries have functioning national distribution systems. Most African firms have had little success in breaking into export markets. Neither newly privatised large firms nor the burgeoning small-enterprise sector has contributed much to improved productive efficiency.

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WHY IS STRUCTURAL ADJUSTMENT NOT WORKING IN AFRICA?

The next question is, 'why should this be so?' Why is structural adjustment not working in Africa? A complete answer is probably not possible with the present level of information, but a return to the elements of the business system provides a framework for analysis. Each of the broad groupings of institutions that make up the business systems of African countries suffers from similar problems that contribute to the fragmentation of the system, and hamper the workings of adjustment programmes: lack of consistent policy development and implementation, lack of accountability, little recognition of the importance of institution building.

One reason for the failure of the structural adjustment policies to achieve their goal appears to be the piecemeal and inconsistent way in which trade liberalisation and deregulation have been carried out in many countries. Reinikka (1996) analyses four consecutive attempts at trade liberalisation in Kenya in the period 1976–92, and shows that they all led to massive speculation because private businessmen were able to anticipate the fate of the reforms. Instead of reducing the possibilities for rent seeking that was the official intention, new niches for rent seeking have continuously been created and distributed through political patron–client relations. In a study of Senegal and Côte d'Ivoire, Boone (1994) writes that 'rather than undermining the rent-seeking logic of accumulation in these countries, liberalising the external trade regime helped to reproduce it'. In both cases the authorities turn a blind eye to quasi-legal and illegal trading activities, allowing politically favoured business groups to escape the full burden of commercial taxation. A similar process has clearly taken place in Tanzania. The continuous changes in rules and regulations and their inconsistent enforcement create an instability in the economic system which is not supportive of long-term productive investments, but favours speculative trade. At the same time, the growing instability has made the poorer part of the population increasingly dependent on family networks and patron–client relations. Therefore, structural adjustment has not reduced the importance of the economy of affection, as intended, but rather increased it.

A second, fairly obvious reason for the failure of structural adjustment is lack of accountability. In a globalising economy it is increasingly difficult for governments to hold the right people accountable. Even if they want to, governments cannot hold multinational corporations accountable for the social effects of their operations. Local producers,

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traders and consumers have little recourse when they are presented with imported goods of dubious origin and quality. Similarly, donors and international NGOs are in many cases more accountable to those providing them with money than they are to the people whose lives they touch every day. Therefore, although both DFI and donor support may be part of the solution to Africa's problems, they are clearly also part of the problem. We need to look at both DFI and the donor support in a much more differentiated way than has hitherto been done. Some of the implicit conflicts are apparent in the current discussions of donor and trade conditionalities on labour and environmental issues.

The lack of mechanisms for holding people accountable is related to an increasingly pervasive feature of African economies: rent seeking and corrupt practices. Illegal rent seeking, corruption and official harassment increase business expenses.[6] Because harassment of small enterprises can be politically motivated and unrelated to a business's legal status, it also adds to the general instability of the business environment. Both the direct payments and the indirect coping strategies required of the enterprises are likely to cut into their profits and productivity.

Nevertheless, it is important to distinguish such destructive rent seeking from profitable trade. The economic environment of African societies, as of rural societies in general, is unstable and risky. Agricultural production and prices are influenced by both seasonal and climatic cycles and swinging world market prices. Lack of physical and social infrastructure and of efficient law enforcement increases the problems. Therefore, even the best of policies to contain the problems of speculation and rent seeking are unlikely to eliminate the possibilities for obtaining excess profits from trade (Fafchamps 1994). And clearly traders moving, for instance, grain from surplus to deficit areas are performing a useful social service even if they earn a large profit.

Even traders whose actions are questionable may perform positive functions in linking otherwise isolated fragments of the business system. In her study of Senegal and Côte d'Ivoire, Boone (1994) writes:

> Mouride commercial networks, Mouride urban transport networks, and Mouride artisanal workshops making shoes and garments organise a section of the urban population into social hierarchies that are linked, at the top to leading *Marabout* who offer the support (and votes) of their followers to the regime.

Despite their undisputed involvement in tax evasion and smuggling, the Mouride traders seem here to provide the link between the artisanal

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producers and the market which seems to be missing in Côte d'Ivoire, as in most of Africa.

The final and, perhaps, most important reason why structural adjustment seems not to be working in most African countries is the lack of concern for forging supportive economic, political and social institutions. Aryeetey *et al.* (1997) trace the continued fragmentation of financial markets in Ghana, Malawi, Nigeria and Tanzania to those countries' failure to pay sufficient attention to institution building. Lack of appropriate institutions means that potential participants in the financial markets lack information and are exposed to undue risks. As a result, markets fail to grow and/or deepen. This analysis probably applies as much to the markets for goods and services as it does to financial markets, though there has as yet been little research on this subject.[7] The problems created for industry by lack of appropriate contract and enforcement mechanisms have already been discussed. Gaps or rigidities in economic institutions governing firms and labour organisation are equally problematic (Williamson 1985). Weak political institutions encourage clientelism and rent-seeking (Putnam 1993), and failure to build new social institutions supportive of technological development, will certainly slow the process of industrialisation (Lall 1995).

The picture painted by this foray into African business systems is far from complete. For one thing, the discussion emphasises the commonalities among the systems and glosses over each national system's distinctive features. For another, the analysis is based on a large number of separate studies, most of which were not designed to describe the national business system of the country in which they were carried out. Clearly, more research is needed. Only with a more comprehensive understanding of national business systems, and their place in a globalising world, will policy-makers and the business community be in a position to move the industrialisation process forward.

NOTES

1 An earlier version of this paper was presented to a workshop on *Business Systems in the South* at the Copenhagen Business School, 22–24 January 1997, and at a conference on *African Business Systems: Institutionalising Industrialisation in the Era of Economic Reforms*, 4–6 June 1997 in Mombasa, Kenya. We are grateful for the comments received in both of these fora.

2 Using data from Kenya, Grosh (1988) challenged the view that manufacturing parastatals are less efficient than private enterprises. She acknowledged, however, that her study was limited by its small sample size and by the fact that it was conducted during a recessionary period.

3 The 1989 population census put the Kenyan Asian population at 0·25 per cent of the total Kenyan population (Kenya 1995).

4 Lall (1995) points out that what is often referred to as structural adjustment really has two different components. One is macroeconomic reform or 'stabilisation', and the other is true 'adjustment'. This article is talking mainly about the latter.

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5 Published information showed over 16,000 workers, but our own independent verification through Kenya's Export Processing Zones Authority yielded a figure for total employment of 14,717.

6 According to K'Obonyo *et al.* (1998) the costs of threats and actual closures and confiscations of goods are significant.

7 One fine example is Ensminger's (1992) study of the institutional transformation of the Orma, a pastoralist community in Kenya.

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