IPPRED-6

The Interdepartmental Action Programme on Privatization, Restructuring and Economic Democracy

Small enterprise development as a strategy for reducing the social cost of restructuring and privatization: Public and private initiatives

Clare Tawney and Jacob Levitsky

Note: Working Papers are preliminary documents circulated informally in a limited number of copies mainly to stimulate discussion and critical comments.

International Labour Office - Geneva - October 1997

ISBN 92-2-110891-0

First published 1997

ILO publications can be obtained through major booksellers or ILO local offices in many countries, or direct from ILO Publications, International Labour Office, CH-1211 Geneva 22, Switzerland. Catalogues or lists of new publications are available free of charge from the above address.

Printed by the International Labour Office, Geneva, Switzerland

Preface

This paper is part of a series of working papers published under the ILO's Action Programme on Privatization, Restructuring and Economic Democracy for use by governments, workers' and employers' organizations, development agencies, consultants, academics and managers. The ILO is particularly interested in the social aspects of privatization, structural adjustment and economic transformation. However, it is also concerned with helping all stakeholders better understand and assess the economic, political and cultural conditions that lead to the successful implementation of these reforms. Experience has indicated that in the areas of privatization and economic transformation, countries that can effectively involve important stakeholders in the process are more successful.

Enterprise restructuring is often an integral part of the privatization process and frequently results in extensive redundancies. There is therefore increasing interest in promoting socially responsive restructuring by combining restructuring decisions with various programmes of retraining and support for small enterprise-creation programmes aimed at those among laid off employees who have potential as entrepreneurs.

This paper aims at reviewing experiences and lessons learned to date about the scope and impact of small business-creation programmes for employees made redundant through enterprise restructuring, including those resulting from a process of privatization. The study shows that the success of the business-creation programmes depends on numerous factors and that the provision of training and finance need to be supplemented by other efforts. Subcontracting and assistance with equipment and premises, are examples of what large companies have done to support small businesses that have been spun off as a result of restructuring. The paper summarizes experiences made in Europe, North America, the former Soviet Union and developing countries and concludes with recommendations for five different strategies for reducing the social cost of restructuring.

Max Iacono,
Action Programme Coordinator for Privatization,
Restructuring and Economic Democracy
International Labour Office, Geneva

Contents

Acknowledgements

The authors would like to thank the following people who supplied information and their time to answer questions for this study: members of staff of the ILO; Julia Johnson of the Department of Trade and Industry; Dr. Ian Pearce of Durham University Business School; David Spence of the British Know-How Fund; Dr. Shailendra Vyakarnam of Nottingham University Business School; David Knox of the British Council and Elizabeth Wallace of the European Bank for Reconstruction and Development.

Executive summary

Since the 1980s, unemployment has been the scourge of the economies of Western Europe and North America, reaching above 20 million in these countries. It is not that the market economies had not known recessions and unemployment before, but the pace of industrial restructuring and technological advance quickened in these latter years, causing mass redundancies resulting in accelerated growth in the jobless numbers. The countries of Eastern and Central Europe and the former Soviet Union have suffered enormous economic and social upheavals as they have struggled in their transition to market economies. Massive unemployment and underemployment began to appear for the first time for several decades in these countries.

Large corporations were closing down or radically downsizing, causing great economic damage and rising unemployment in communities that depended to a considerable extent on these companies for their welfare. It has been recognized that these companies, on which whole communities have depended for a great part of their economic livelihoods, owe a debt to mitigate some of the effects of their restructuring actions. More and more, large corporations have developed, with government and regional assistance, programmes specifically focused on creating new employment opportunities to replace the jobs lost.

In the United Kingdom, the wholesale closure of steel mills and coalmining operations in the period 1970-95 exacerbated by job losses accompanying the privatization and restructuring of enterprises in these and other sectors, spawned special programmes to revive the abandoned collieries and steel towns. Likewise, in France, major restructuring initiatives of large basic industries — glass, oil and gas, metals, electronics — that had previously been major employers in different areas of the country, launched initiatives to foster business development that could replace the employment opportunities lost.

One feature that became quickly apparent was that in virtually all cases, existing employers in the area affected could not possibly provide sufficient numbers of new jobs to employ the workers made redundant. New businesses had to be created, preferably initiated by redundant employees themselves to create new employment. The lack of business skills and, in most cases, the specialized character of the previous work experience, required programmes of intensive training, particularly in business management techniques but also, in many instances, in new technologies as well.

Neither training alone, nor even advisory services through business centres set up to help potential entrepreneurs to prepare business plans, generally result in quick "start-ups". Finance is a vital ingredient which most redundant workers lack. Their own resources are limited and they have few ideas on how to access funds from banks. In most support schemes, financial help is needed in various forms: loans, grants and equity investments. Public funds are required together with some additional financial assistance from non-public sources in many cases made available as credits and/or equity from the former employer or from local businesses.

Financial help is not only available in the form of capital assistance. In some cases, the former company employers offer vacated premises, used equipment and guarantees for orders or for bank loans. Where there has been restructuring which has outsourced services or items previously made in-house, an arrangement is negotiated for the new small business to carry out these operations as a subcontractor. Help may also be offered to obtain further orders from other firms to help launch the business.

More radical measures have to be taken both by government, regional authorities, financial institutions and large enterprises where large-scale privatization is being carried out, as in the former communist countries of Eastern and Central Europe. In the example of eastern Germany, the public authorities involved decided on major intensive measures, such as creating special employment companies to assist in the transition. These companies combined both training programmes, short-term working projects and acted as temporary employers of the retrenched workers.

There are various forms of support that can be offered by large firms to new and expanding small businesses, many of which are of immediate and/or long-term commercial benefit to the company. Locating new or better suppliers or subcontractors in the vicinity is, of course, the most direct. Generating employment or business opportunities for workers' families in new local small business development can be an important stabilization factor for the company's workforce. Assisting local businesses can do a great deal to improve a company's image and can help motivate employees as well as generate better relations with local and central government which can be of long-term value in various ways. Not least, in some cases of regional collaboration with small businesses, there can be direct advantages in wider retail distribution and enhanced marketing outlets.

Support to subcontractors and to various forms of forward linkages can involve technical assistance, help in finance, assistance with tools, equipment and premises and, in some cases, forming groups of small businesses to improve outlets (see the cases given in the annexes on Hoechst SA and the automobile cluster in Baden-Württemberg, Germany).

In the former communist countries, spin-offs from restructured large enterprises provide major small business opportunities (see case of Prompribor, Russian Federation) but are difficult to develop without considerable help from the parent enterprise. Privatization can slowly "hive off" many activities — both services and product inputs — that in the former regimes were performed in-house.

Developing countries provide fewest opportunities, as there are both fewer suitable large enterprises and a weak small business sector. However, a large unemployed and underemployed population and a thriving informal sector in many such countries can be a reservoir for potential entrepreneurs which, with appropriate public and private assistance, can burgeon into an expanded local small business community.

Several large multinationals have begun to recognize the need to help promote local SMEs even if only to provide the services and inputs they need to carry on their business successfully. There is also a new consciousness among MNCs that to receive collaboration and favourable treatment from developing country governments, they have to show they are contributing to developing the local economy and to improving the quality of life of the population. Where there exist substantial indigenous larger companies (e.g. India, Philippines) there are movements among these to support local SME development as well.

One of the instruments used to save an ailing business is through a "management buy-out" (MBO). In the United States where MBOs have been most prevalent, they are part of the movement to create ESOPs (Employee Stock Ownership Plans), a form of employee participation in the equity of a firm. Some cases are described of ESOPs and MBOs from the United States and the United Kingdom (where next to the United States, most MBOs have taken place). Usually the management (and often all employees) buy out the whole troubled firm to save their jobs and make concessions on employment, pay and/or benefits. The commercial results vary. Some MBOs, particularly in the United States, have not only saved their jobs but have made significant capital gains for the employees concerned. In the United Kingdom there have been firms — particularly in the transport industry e.g. National Freight — where the employees made such large gains that there were allegations that the firm had been undervalued and sold off cheaply.

In Europe, the United Kingdom is far ahead in the number of MBOs in the period 1980-89; 2,992 as against France (430) and the Netherlands (245). This is probably due to more developed venture capital availability, more opportunities in the privatization of publicly owned enterprises and the restructuring of large businesses, and the more developed capital markets so that "exits" are more feasible. MBOs also take the place of "unwanted" divisions or activities of parts of an enterprise leading to smaller businesses.

Venture capital plays a major role in MBOs, since the employees involved rarely have the capital resources nor can raise sufficient bank loans to complete the transaction. Venture capitalists coming in with 20-30 per cent (always a minority) usually help solve the financing problems. Favourable taxation for buy-outs, as in the Netherlands in the early 1980s, also encourage MBOs. Work councils have made it difficult for unwelcome outside bidders to succeed in some European countries. Sweden had a flurry of successful MBOs in the period 1988-90 helped also by a favourable tax and legal regime and the need to restructure large firms. In some European countries — Germany and Italy — there are problems of large numbers of small and particularly medium-sized family businesses where there are major succession problems which have hampered the development of MBOs, but in both these countries MBOs have increased in the early 1990s.

The encouragement of LBOs (leveraged buy-outs, which are MBOs where the debt-related instruments and loans from banks constitute a majority of the capital raised) leads to extra motivation of the managers and employees to defend their equity stake. In the early 1990s the deep recession in the United Kingdom and then throughout Western Europe, produced a number of buy-outs of SMEs in receivership.

In general MBOs result in a substantial fall in employment. According to studies (Wright, et al., 1992) there are initial "shake-outs" of employment and the companies remain leaner in this respect than other firms in the same sector.

1. The United Kingdom

Categorizing the people involved in restructuring

The conceptual framework of this paper is based on the people who have already lost their jobs, or who are in danger of doing so, as a result of the privatization or restructuring process. It is the loss of security facing such people that constitutes the "social cost" indicated in the question; and it is the people and their talents who offer to a varying extent the potential of creating new businesses and new employment.

Retrenched workers may be divided into the following categories:

- those who are persuaded to take early retirement;
- those who remain in long-term unemployment;
- those who manage to find alternative employment;
- those who choose to become self-employed or to start a microenterprise; and
- those who are involved in launching a formal small business with potential for growth.

This paper does not deal with the first two categories; neither is alternative employment the principal focus of this study: in a locality or a country where increasing numbers are losing their jobs, the numbers applying for any new posts are bound to be high. However, alternative employment is the preferred and only conceivable option for many people, and in fact one outplacement agency suggested that only between 6 and 10 per cent of its clients chose self-employment or starting a small business as opposed to finding a new job.[1] Helping its former employees into jobs in other companies is clearly the main concern with many companies facing restructuring.

The main focus of study is job creation through developing new economic opportunities: either through self-employment (or the creation of micro-enterprises),[2] which requires only a limited amount of entrepreneurial flair, but also hardly creates any new jobs per business; or through assisting entrepreneurs to launch small businesses with greater growth potential. This last category will probably comprise the smallest number of people in any cohort leaving employment, and it may need the largest amount of resources per capita, whether in terms of finance or business counselling. However, small businesses with growth potential hold out the promise of employing more people, providing diversity in the local economy, and stimulating economic growth. The origins and needs of small, fast-growing businesses are also rather different from micro-enterprises: they are usually started by people with managerial or business experience, and it has been argued that they are often started by management groups, rather than by individuals.[3] Such small businesses may be formed around a novel business idea, or a new way of operating, and they may require more help from experienced business consultants than would self-employed people, for whom it is easy to "start-up".

Small businesses v. self-employment

The Business Start-Up Scheme that was operating in the United Kingdom in the early 1990s under the Training and Enterprise Councils aimed to support people who had been made unemployed and were entering self-employment with an enterprise allowance and with business

[1] From a conversation with the Managing Director of Grosvenor Career Services, 1997.

[2] "Self-employment" and "micro-enterprise" are used interchangeably here; even though one refers to the fact that there is only one job involved, whereas the other is defined by measures such as sales turnover, and might include one or two additional employees.

[3] Vyakarnam and Jacobs, 1993.

advice and training. The scheme was criticized for the high failure rate of the businesses thus supported, however, the feeling being that at least some of the resources could have been put to better use in supporting growth-oriented businesses. In 1993 the expected number of new businesses started in the United Kingdom was 350,000, creating an average of 1.5 jobs in addition to the owner; however, the number of businesses failing was 50,000 per year.[1] Self-employment is not only precarious, it also results in low incomes. Evidence taken from US studies of different approaches to job creation for retrenched workers suggests that the demonstration project offering business training for self-employment compared favourably with projects offering retraining for re-employment, but the average income resulting from self-employment was lower than a living wage.[2]

While low initial incomes and high failure rates are to be expected from any kind of business start-up, it would be desirable if the businesses that did survive included some with a high potential for growth. Studies from the United States demonstrate that one ingredient for success is team work: almost two-thirds of the youngest of the Inc. 500 companies started in the 1980s were started by teams.[3] Brockaw also quotes a study of "hyper-growth" businesses which found that only 6 per cent of the ventures were founded by a single person; whereas 54 per cent had two founders and 40 per cent had three or more.

Accepting that high growth-potential businesses are often started by management teams, it is still unclear how management teams come together, or how their formation can be assisted by outside agencies. However, where a group of people embarking on a business start-up has already had the experience of working well together in their former employment, some elements of team work have already been established. This situation can arise when management teams have been made redundant following the restructuring of a business, and it often does take place during management buy-outs of part of the restructured firm, or spin-offs of small businesses from the core enterprise.

In the course of this study, where it is possible, attention will be focused on whether the measures that have been used to stimulate small businesses have been successful in promoting growth-oriented small businesses as well as self-employment. What follows is a number of examples from the United Kingdom of types of support programmes for redundant employees which have been adopted by specific companies or agencies, and with what results.

British Steel (Industry)

One of the first job-creation companies set up by a commercial organization in Europe was British Steel Industry.[4] In 1975, when British Steel Industry (BSI) was established, the privatization process had yet to begin in the United Kingdom. At that time steelworks were operating in 20 areas of England, Scotland and Wales, but were being restructured to facilitate the sale to the private sector with large numbers of redundancies in the process. Some whole towns and areas suffered economic devastation.

BSI's small business-creation schemes are not aimed exclusively at former steel employees, but concentrate on any business with growth potential which chooses to start up or relocate into one of the 20 defined steel employment catchment areas. Most redundant steel employees prefer to seek alternative employment or else self-employment, than to start a small business of their own. BSI has attempted to improve the employment options of former steelworkers by stimulating the growth of new businesses in the steelworking areas.

[1] Vyakarnam and Jacobs, 1993, citing Bradford, and *The Guardian*, 1992.

[2] Drury, et al., 1994.

[3] Brockaw, 1993.

[4] British Steel Industry (1996).

The two main thrusts of BSI's activities are financial assistance and the provision of managed workspaces. In 1975, when British Steel Industry (BSI) was established, few of the small business support services now in operation were in existence, and at that time BSI provided an advice service for small businesses. This work has been phased out now, the assumption being that this is best handled by local enterprise agencies, Business Links, or other such agencies.

Managed workspace

BSI currently provides 357 light industrial and office workspaces at eight locations within the steel areas. The features that make them suitable for small businesses, particularly "start-ups", are that they incorporate a wide range of services and facilities, enabling the small business person to concentrate on production. Also, occupancy is on a short-term lease, which means that when the business has outgrown the premises it can move on to a new site without the burden of a longer-term commitment. Between 1975 and 1996 BSI had invested over £12 million in managed workspace, and 1,350 small businesses had benefited from these facilities.

Table 1. Businesses supported by BSI

	Percentage financed	Percentage occupying workspace
Sector		
Manufacturing/engineering	71	59
Services	12	36
Other	17	5
	100	100
State of development		
Start-up	27	78
Expansions	63	16
MBO/MBI	6	0
Other	4	6
	100	100
No. of employees		
1-20	59	-
20-99	38	-
100 or more	3	-
	100	

Source: British Steel Industry (1996): *Twenty-one years of going for growth.*

It is clear from table 1 that the workspace component of BSI's support is aimed mainly at start-ups, with small workforces (93 per cent employ up to ten).

Finance

BSI provides loans and equity to businesses with good prospects for growth within the steel areas. More often this assistance is aimed at expansions rather than start-ups, but nevertheless the relatively small amounts involved — loans between £10,000 and £150,000, and venture capital between £25,000 and £150,000 — make this source of finance attractive to small businesses. The loans are typically for a three to four-year term, with fixed interest rates. Equity capital can be taken up on its own, or in a equity/loan package, such that the BSI share of the investment is less than 20 per cent of the company's equity. BSI is willing to give management advice if requested, but leaves the day-to-day running of the business to the management.

Investments have included helping the "turn-around" of established businesses by financing management buy-outs.

BSI was one of the first United Kingdom corporate organizations to provide venture capital in amounts below £100,000. Through its share capital and loans schemes, BSI has provided £31 million of finance to 1,600 businesses, plus a further £11 million of support in the form of business consultancy and grants (which have now been discontinued).

Indicators of success. Taken together, BSI's workspace provision and finance have supported 3,500 businesses in the former steel towns during 1975-96, and BSI estimate that this has involved the creation of 58,000 jobs, or an average of 17 jobs per business supported.[1]

BSI gives a general figure of 80 per cent as the average survival rate of businesses they have financed, emphasizing however that this rate was lower in periods of recessions and is slightly higher today. BSI's investments include a large proportion of manufacturing and engineering businesses (see table 1). At the same time as concentrating on growth-orientated, job-creating businesses, with a reasonably high survival rate, amongst these BSI have managed to channel over one-quarter of their investments into start-ups.

British Coal Enterprise

As in the case of British Steel, when a series of redundancies and pit closures were put into operation in the 1980s and early 1990s, large numbers of mineworkers found themselves without jobs in communities which had been dominated by the coalmines, and possessing skills that now had no outlet. British Coal Enterprise (BCE) was launched in 1984 and, like British Steel (Industry), it concentrated on supporting the economic regeneration of areas which had been affected by closures, in the hope that new businesses, whether run by former coal employees or others, would provide employment opportunities for those made redundant. The three principal areas of BCE's operation were: business funding, workspace provision, and outplacement services.

Finance

Fast-track loans of up to £25,000 were made available to start-ups and small businesses within the seven coalmining regions defined by BCE.[2] In addition, for larger start-ups and expanding businesses, an Enterprise Fund was set up providing venture capital investments of up to £250,000. BCE also managed funds from other sources, targeted on specific areas within the coalfields, and totalling £3 million.

Indicators of success. The total investment made by BCE during its existence (1984-96) was £101 million in over 5,000 enterprises, generating 50,024 jobs.[3] A further 4,600 jobs were expected as the current investments matured, making an average of 11 jobs created per business. Overall, BCE estimated the cost in investments per job created to be £1,384. An analysis of the

[1] British Steel Industry (1996). These estimates are based on forecasts of the numbers of jobs that would be created over a three-year period that were made at the time of investing in the businesses. A survey based on a random selection of these businesses compared these forecasts with actual numbers of jobs, and found them to be very reliable.

[2] This and much of the following data comes from British Coal Enterprise (1996).

[3] These figures are taken from BCE (1996). Coalfields Investments' Director reports that estimated numbers of jobs expected were provided by SMEs when applying for finance, and actual figures were recorded during follow-up visits, and when the loans were repaid. A follow-up study showed that the actual numbers of new employees resulting from the investment generally exceeded the original investment by about 25 per cent (pers. comm., 1997).

types of job created by sector is given in table 2; 61 per cent of jobs are in sectors other than manufacturing.

Table 2. Jobs created as a result of business funding by BCE

Sector	Percentage of jobs
Minerals and chemicals	7
Other manufacturing	32
Construction	5
Distribution and repairs	18
Transport and communications	3
Banking and insurance	9
Other services	26

Source: British Coal Enterprise, 1996: *The enterprise years.*

Of the approximately 50,000 jobs created during the period 1984-96, 56 per cent derived from business start-ups, and 44 per cent from business expansions. During this period, when business start-ups were considered, only those with considerable promise of growth received funding, and this policy has resulted in a high proportion of the jobs created arising from business start-ups: these were not micro-enterprises, employing one or two people.

The business funding arm of British Coal Enterprise was sold to a management buy-out in 1996, and the new company, Coalfield Investments, continues to invest in small and medium businesses in the coalmining areas. Now that Coalfield Investments is fully commercial, and concentrates as much on making a profit for its financial backers as fulfilling its obligations to British Coal to create jobs, it no longer finances business start-ups. This policy is based partly on the fact that there is no longer any government or European Union subsidy for start-up finance, and partly on its experience that 30 per cent of start-ups ended in failure, as against less than 20 per cent of business expansions.[1]

BCE's funding arm provided advice during the setting up of similar ventures in Poland, under the British Council's Polish-British Enterprise Programme (see section on Poland), but now concentrates exclusively on investments in the United Kingdom.

Workspace

Based at a total of 51 sites, 1,121 units have been built with European grant assistance. The "easy in — easy out" terms of the leases of the units are aimed at the needs of new and growing businesses in the coalfields. It is estimated that a total of 16,200 jobs have resulted from BCE's provision of workspace.

Outplacement

During 1984-96, BCE's outplacement division managed the largest resettlement operation in Western Europe.[2] British Coal Enterprise's Job and Career Change Scheme (JACCS) helped approximately 60,000 redundant coal employees back into work, by providing one-to-one counselling with career consultants, help with CV preparation and with proactive job-search techniques. In addition, where necessary British Coal paid for retraining.

In 1992, the Government announced that it was going to close down a large number of collieries, and it was between October 1992 and December 1995 that Grosvenor Career Services

[1] These last figures were given during a conversation with the Director of Coalfield Investments (1997). The overall failure rate of businesses receiving funding by BCE was 23 per cent.

[2] Welch (1997).

(the name for the commercial division that had grown out of JACCS) had responsibility for resettling 33,059 coal employees: the largest wave of redundancies. Grosvenor reports that 87.5 per cent of these had been resettled by the end of 1995 (either in new jobs or setting up their own business); the remainder were either still looking for work or had dropped out of the scheme. They cite this as a particularly difficult outplacement project, partly because many coalminers had skills that were not transferable outside the mining industry, and partly because there was some resistance among employers to taking on new staff with a reputation for unionized militancy.[1] Nevertheless, an independent survey carried out in 1995 revealed that approximately one-third of coal workers had found a job at a higher salary; one-third had found work at the same salary, and one-third had taken a drop in salary.

Grosvenor's evidence seems to suggest that the majority of employees found new jobs. However, the economic buoyancy in some areas has to be set against a more depressing picture in other localities: in the valleys of South Wales, for example, where approximately 40,000 miners were made redundant, male unemployment is still well over 20 per cent, several years after most of the pits were closed.

In 1996, Grosvenor Career Services was sold to a management buy-out team, and now provides outplacement services to a variety of large companies undergoing restructuring, as well as employees leaving British Coal. Their clients have included British Nuclear Fuel, British Gas, British Rail, Tate and Lyle, Liverpool Victoria Friendly Society, Kimberly Clark, and many other public and private bodies undergoing restructuring. Grosvenor has also provided expertise in outplacement in coalfield regions in a number of European countries, including Poland, Uzbekistan and Ukraine, where it is advising on labour market restructuring under the EU's PHARE programme.

Support for business start-ups. According to Grosvenor's Managing Director, between 6 and 10 per cent of employees interviewed are interested in self-employment or starting up small businesses, as opposed to finding employment elsewhere. Grosvenor was also involved in running outplacement schemes for former employees of British Telecom, after the restructuring of its workforce following privatization. Of the total number of employees who chose to take part in small business counselling, help in preparing a business plan and follow-up monitoring and business advice, 75-80 per cent successfully launched their businesses.[2] According to a follow-up survey conducted two years after the start-up, 70 per cent of these businesses survived.

Occasionally Grosvenor is able to deal with teams of employees who wish to continue to work together either to start up a new business or to continue in their existing line of business through a management buy-out, one example currently taking place being a management team within the construction company, Balfour Beatty. However, such occurrences are not frequent, and most employees opting for starting a small business are doing so on their own.

The payment for outplacement services, such as those provided by Grosvenor Career Services, is generally met by the organization undergoing restructuring — British Coal, in the case of the mineworkers — and is calculated according to the number of individual interviews, group workshops or monitoring sessions provided.

Government support for start-ups

Although the United Kingdom's Business Start-Up Scheme (BSUS) has largely been phased out, it is worth mentioning, partly because it is still in existence in some regions, and partly because schemes like it are still in operation in most of Europe. Although the exact details depend

[1] ibid.

[2] Taken from a conversation with David Pickering, Managing Director of Grosvenor Career Services, 1997.

upon the design favoured by different regions, generally the BSUS allowance of £40 per week over one year was available for people who had been unemployed for a number of weeks, and who wanted to start up a new business or become self-employed. (The amount is now equivalent to £40 for 13 weeks where the scheme is in operation.)

The finances are handled by the local TEC (Training and Enterprise Council), which receives the initial application, discusses it with the applicant, and if the business idea seems worthwhile, accepts the applicant on to the programme. Local enterprise agencies (see below) usually receive the contract for providing pre-entry business counselling and training. This covers business skills training (bookkeeping, pricing, marketing, etc.) as well as help in preparing a business plan. Participants are obliged to attend all of this training and submit an approved business plan usually before their first allowance payments are made. In some areas the allowance is "front-end loaded" to help with start-up costs and the purchase of equipment; however, some financial incentives are kept back to induce participants to attend follow-up monitoring sessions at 4 and 7 months.

In 1992 the administration of the support schemes for growth-orientated businesses was transferred to the Department of Trade and Industry, while the Department of Employment retained the Business Start-Up Scheme for micro-enterprises, which has subsequently largely been phased out.[1]

Business support agencies

LENTA

The London Enterprise Agency (LENTA) is a private sector organization which was set up in 1979, and from that time has been involved in the provision of business workspace in the capital. In 1994, LENTA launched "Investment Saturday", which was a day-long introduction to running your own business, and was followed by help in preparing a business plan, and business advice. "Investment Saturday" is aimed at managerial-grade employees, and many of the 400 people who have received this training have been funded by their current employers, who are undergoing retrenchments. For example, London Dockland Development Corporation have financed the training of 36 of their employees, and London Underground's Jubilee Line Extension team have sent 30 of their employees for training.

A recent evaluation of "Investment Saturday" showed that 33 per cent had already started a business, 21 per cent were currently working on their business plan, and 25 per cent had made no progress in starting a business. LENTA also provides business consultancies and direct small businesses with growth prospects towards sources of venture capital finance.

MADE

MADE, a private sector company supported by public finance, has a number of offices based in the coalmining valleys of south Wales, and was formed in 1984, when pit closures were first starting, following a period of industrial action. Previously coalmining provided 40,000 jobs, and now only one pit is still working, employing 300. Male unemployment is still at 25 per cent in the region, and is even higher in some of the former mining towns.

MADE provides free business advice for start-ups, helps in the writing of business plans, arranges business training, provides workspace for small businesses, refers start-ups to sources

[1] In England, the Business Start-Up Scheme was subsumed by the Department of Environment's Single Regeneration Budget. The authorities of depressed areas can apply for funding for projects from this budget, and these projects might include incentives to attract businesses into the area. It is not known, however, how much is available specifically for business start-ups.

of funding, including local authority seed capital (£1,000-£5,000), maintains an equity fund and advises larger businesses on how to access larger amounts from banks and venture capital, including potential private investors ("business angels").

MADE claims that in 1996 through its professional advice it was able to assist in the creation or safeguarding of about 1,200 jobs. This agency covers a region where the former British Coal Enterprise and British Steel (Industry) operate their business finance schemes, and MADE helped a number of businesses secure funding from these sources, which together with local authority and bank funding amounted to £3 million in 1996. Since its start in 1984, MADE has assisted businesses to achieve over £17 million in investment in the region, and has played a part in creating or saving nearly 10,000 jobs.

MADE is now funded largely through its property portfolio (renting out business units) and partly through its contract to the Mid-Glamorgan TEC to provide business start-up advice and training. Periodically it bids for European assistance. MADE has also been able to share its experience of working in a declining coalmining area, by hosting a staff member from the Hungarian Foundation for Enterprise Promotion.

Indicators of success. In 1996, MADE gave 2,010 business advice sessions for start-ups; and, helped in this relatively minor way, 301 businesses, employing 372 people, were started up. According to MADE's analysis of business start-ups in 1995, the business survival rates were 84 per cent for those receiving Business Start-up Scheme funding and 81 per cent for those without it (measured 12 months after the start of trading). These are fairly high rates;[1] however, some caution has to be exercised since the Mid-Glamorgan TEC's analysis for an overlapping area gives business survival rates in 1996 of 78 per cent for the first year and 65 per cent for the first 18 months. Differences between the figures can often be attributed to regional variations or to periods of recession affecting the businesses.

What is more interesting is the interpretation put upon the figures by the organizations themselves. One innovation that is about to be introduced by the Mid-Glamorgan TEC as a result of observing impressive business survival rates from another support organization, the Prince of Wales' Business Trust, is the mentoring of the new business. Instead of all the training and business planning taking place at the MADE office, business advisers will visit the site of the new business, where it is anticipated more of the problems facing the business will become apparent.

Business Links

This initiative is aimed at small and medium enterprises (SMEs) with growth potential (typically with ten to 200 employees), rather than at micro-enterprises. The emphasis is on help with innovation and technology upgrading, and with exporting, all key concerns with businesses hoping to expand, and provide more employment, rather than micro-enterprises providing a single, low income in a business area in which there is considerable competition. Each business is provided with a Personal Business Adviser (PBA), who helps to refer SMEs to a range of services, such as: innovation and technology counsellors; export development counsellors; access to the Regional Supply Network, linking businesses with local suppliers; training courses; business "health checks"; and referrals for business funding, including venture capital.[2]

PBAs can advise on local and regional assistance, such as pump-priming grants, assistance with the purchase of capital equipment, or for supporting an initiative which will take on more employees. Such assistance varies according to the part of the country: highest priority is given to certain regions suffering from high unemployment, such as north-east England where much

[1] The difference between the two amounts is quite small, reflecting either that the Business Start-Up Scheme has little effect on survival rates, or that the people that did not benefit from the allowance had more personal finances to invest since they had not been unemployed for some time.

[2] Business Link (undated).

heavy industry has been restructured and closed down, and these regions receive European funding support. Businesses, including SMEs, moving into such areas may qualify for rate and rent holidays or other incentives.

The National Linkage Programme, Ireland

Another initiative aimed at stimulating and upgrading SMEs rather than micro-enterprises is the National Linkage Programme, which is responsible for helping Irish companies win increasing business by meeting the purchasing needs of multinational companies and other major purchasers based in Ireland. These needs might include local construction companies being involved in the development of infrastructure, where multinationals have chosen to relocate to green-field sites; the aim would also be to enable foreign-based companies to source their supplies from Irish firms (not necessarily small firms), rather than to import them from the country of origin.

The National Linkage Programme was launched in 1985 as part of the Government's White Paper on Industrial Policy.[1] It is co-funded by Forbairt (the Government's industrial development agency), and the European Development Fund, and is structured on a sectoral basis (the areas being electronics, health care, consumer products, engineering, construction and public sector) and on a regional basis. Key elements of the programme are:

- *Information brokerage*. Existing and new multinationals in Ireland, together with Forbairt overseas offices, are briefed on Ireland's sub-supply capacity via presentations, newsletters, mailshots, and so on. In addition, technical profiles of more than 750 supply companies are now on the Internet.
- *Supply development initiatives,* designed to improve the capability and competitiveness of supply firms.
- *Groups structures* are encouraged to meet customer demands.
- *Technology partnerships/overseas partnerships* are developed to address gaps in technical capabilities.

Indicators of success. In a number of sectors covered by the Linkage Programme the growth in performance has been considerable. The major Irish supply companies to the electronics sector had excellent growth in 1995, with output increasing from £315 million to £420 million, and exports increasing from £61 million to £87 million. The construction linkage companies and the health-care/consumer product linkage activities generated more than £20 million in new business for over 90 Irish supply companies in 1995.

Ireland's National Linkage Programme does not relate directly to the problem of retrenchments following restructuring, but is aimed at mitigating the general high unemployment in this country. However, foreign-based companies have often chosen to base their industrial operations in regions that have previously been dominated by heavy industries before restructuring or privatization, and where there are skills available. This is so of Korean, Japanese and American businesses in the valleys area of south Wales, where improved road networks and business support infrastructure have helped to improve the industrial potential of the area. Efforts to build supply linkages between incoming multinationals and local companies could make a significant impact on the growth of local SMEs, thus creating more employment in areas where many have been made redundant.

Management buy-outs and spin-offs

These strategies have perhaps the greatest potential for retaining jobs, using existing skills and boosting economic growth, while an industry is at the same time undergoing radical

[1] Forbairt (1995).

restructuring. Management buy-outs (MBOs) consist of the existing management team of a firm putting forward a financing package to buy the entire firm; spin-offs result when a large firm is divided into separate cost centres which are then managed as separate businesses.

MBOs often occur when there has been a problem in the succession of a family business; they also arise in about 20 per cent of cases following a firm going into receivership (higher during times of recession). MBOs are the most popular form of privatization among the smaller United Kingdom state-run companies; for example the Scottish Bus Group and many municipal bus companies have been privatized through MBOs. Because of the size of the investment, MBOs are only partly financed by debt; typically, the remaining part is structured so that management make the largest equity investment and a venture capital firm makes a smaller equity investment, thereby ensuring that the management have the largest shareholding in the company. By comparison, spin-offs do not always require major financing, since the parent company sometimes remains as the holding company of the assets they take over.

Indicators of success. A survey of UK MBOs shows that, as in the United States, job losses usually follow the buy-out (an average of 6.3 per cent); however, further jobs are also often created in the years following the original shake-out.[1] In terms of their performance, most buy-outs in the sample did better than prior to the change of ownership (82 per cent had either the same or larger trading profits), as well as doing better than their own business plans.

Conditions for success. The MBO market in the United Kingdom is the second largest in the world (the first being in the United States, and consisting of rather larger, leveraged buy-outs, where the management holds a minority of shares). MBOs are also becoming increasingly popular in France, but elsewhere in Europe the market for MBOs is not equally developed. The conditions that favour the successful operation of MBOs include:

- the generation of opportunities for MBOs;
- suitable infrastructure to complete deals; and
- the availability of suitable exits from the investment.

In order for there to be MBO opportunities, as well as the basic prerequisite of entrepreneurial managers willing to buy their firm, there must be an ownership structure which allows for the sale of the firm. This structure exists in the following cases: a family firm with succession problems; the restructuring of a state-owned firm; corporate groups, part of which could be sold off; and stock market quoted firms.

As well as the opportunity, business infrastructure must be in place to support the change in ownership. This includes, as well as a favourable legal and taxation framework, debt finance and a well-developed equity investment market, and also experienced intermediaries or advisers to help the management team. Venture capital plays an important role in management buy-outs, and it is in countries where it is not yet well developed that there are fewer MBOs, for example Germany. In the United Kingdom, the 3I Group, which is Europe's leading specialist investor in unquoted companies, invested over half of its funds in MBOs and management buy-ins in 1996.[2]

Finally, neither the management team nor the venture capital investors will want to finance the MBO unless there are various exit options for them to realize their gains. These include: flotation on the stock market, a trade sale, further refinancing and a secondary MBO.

An example of a successful management buy-out comes from the field of business support itself: British Coal Enterprise (BCE), whose work was described earlier. BCE was comprised of three departments: outplacement, business funding, and managed workspace, and when in 1996 BCE was sold off by British Coal, although the managed workspace division was bought up by

[1] Wright, et al. (1992).

[2] 3I Group (1996).

Birkby plc, the outplacement division, Grosvenor Career Services was sold to a management buy-out, as was the business investment division, renamed Coalfield Investments. Since 1989, the outplacement division had been carrying out commercial contracts for a number of industries undergoing restructuring other than coal, which made the transition to a completely separate business much easier. They now have 11 regional centres and have assisted over 700 organizations in both the public and private sectors.[1]

What this example demonstrates is that spin-offs and management buy-outs from a privatization or major restructuring can be profitable, and can retain jobs and expertise, as well as keeping management teams intact. It is also clear that where a spin-off has taken place successfully, the gradual evolution over a period of time of separate commercial units within an industry has helped to make the change smoother, with a lower loss of jobs. This can be contrasted with the situation in areas of the world where privatization and restructuring is taking place speedily, and where the market economy is less well-developed (see the section on Romania).

[1] Welch (1997).

2. European countries

France

France has, since the 1960s, been among the foremost countries in developing collaborative relationships and partnerships between large and small businesses. Also on many occasions, governments of different political persuasions and large-scale enterprises, both public and private, have been ready to intervene to help and support smaller enterprises.

Saint-Gobain

A major example occurred as far back as 1979 when the large glass-making corporation Saint-Gobain (SG) set up a special department, Saint-Gobain Promotion, to mitigate the impact of the changes planned for the 1980s. In 1983 Saint-Gobain Promotion became Saint-Gobain Development (SGD) and became the main instrument to help the deployment of personnel made redundant in the major restructuring of the corporation aimed at eliminating loss-making activities, shifting in a massive way to automation and reducing production capacities to a level which the market could absorb. It was concluded that 20,000 jobs would be lost over four to five years through the changes to be introduced, and that a programme was drawn up to help those who lost their jobs to find alternative occupations.

As a result SGD embarked on plans involving both the conversion of the sites — the locations where the major changes would occur — and personnel changes which involved help in redeployment, retraining and possibly relocation of those who would become redundant. A strong element was support for local and regional development in cooperation with the relevant authorities.

The results were very tangible. In four years, 500 agreements were entered into with SMEs, resulting ultimately in the creation of 10,000 jobs. Financial assistance was made available as long-term loans (at half the regular bank interest rate) and without security or guarantees. The financial help, given by SGD, was backed by comprehensive technical aid. By 1988-89, SG had completed its main restructuring operations, but SGD continued to operate, putting more emphasis on strengthening the economic and industrial environment in which the corporation operated and in developing further a whole range of cooperative activities with SMEs, including employment generation, the supply of industrial services, and new forms of subcontracting. SGD has pursued a programme of organizing continuous contacts between the corporation's executives, at all levels, and small business owners in the regions of SG's operations. Assisting the redeployment of staff within the SMEs supported and assisted in "start-ups" continues to be a major function of SGD.

Elf-Aquitane

Another interesting case in this field, going as far back as the early 1970s, is that of Elf-Aquitane (EA), the giant French public oil and gas corporation. In 1972 a capital grant of FF6 million was made available to local financial institutions in south-west France where the company operated in gas fields which were considered to have a limited life, to provide loans to SMEs and to new businesses in the area to absorb those who were made redundant through EA's reduction of its activities.

Later in the 1970s, EA created SOFREA (Societé de Finance Régional of EA) which, by 1988, had granted over 1,000 loans (at subsidized interest rates) to over 830 small businesses at different sites for a total of FF920 million ($140 million). SOFREA helped only those firms planning to start up businesses or to take over existing ones, in all cases involving the creation of new jobs or maintaining existing employment. After ten years of activity, SOFREA claimed to have helped in this way to create or maintain 20,000 jobs. EA also set up in 1980-85 two technology transfer centres for small firms in the south-west region of France.

Elf-Aquitane's policy-makers regard the firm's activities in this field not only in terms of enhancing their image, but also helping to obviate the need to prolong loss-making activities by ensuring continued employment for potentially redundant staff.

Pechiney

A further case in France concerns Pechiney, the large metallurgical corporation which in the 1980s decided to close one of its plants which had been operating in the Pyrenees region for close to 50 years, in order to concentrate production. The closure of the plant was a serious economic blow to the economy of the district, being the only heavy industry working there.

In this case Pechiney cooperated closely with the local public authorities to implement a redevelopment plan. A large, low-interest loan and a large grant were made available from local and regional councils. The redevelopment plan, carried out over a few years by Pechiney, directly helped create two SMEs and together with the local authority who provided guarantees and direct loans of around FF17.5 million helped develop another small enterprise employing over 40 people. The local authority itself also helped the start-up of a small firm preparing ready-packaged meals. Together these SMEs gave work to over 100 employees which contributed significantly to preventing the rapid decline of this rural area after the Pechiney plant closure.

In France some of the larger firms have begun to see the advantages of closer partnership or collaborations with SMEs who, it is recognized, have the capacity and flexibility to adapt quickly and can therefore innovate more easily. In a rapidly changing technological world, if employed effectively, innovation can be an important source of increased competitiveness.

Thomson

An example of where the above considerations played a role was that of Thomson, the large electronic corporation. In 1987, facing fierce competition from Asian suppliers, Thomson decided to close its microcomputer plant in the village of St. Pierre (population 2,000) in central France, with the loss of 550 jobs. A consulting organization, GERIS, was given the task of finding firms that could use the St. Pierre site that Thomson was vacating and so replace the jobs lost and help prevent the economic and social decline of the area where there were few other industrial employers.

GERIS made contact with the electronic firm SOFREL with 190 workers located about 100 km from St. Pierre which showed keen interest in taking over the site. SOFREL and GERIS worked out the details of a project which could, it was agreed, provide employment for up to 250 persons in three years, starting production in 1988 with 60 workers engaged in specialized electronic subcontracting. As SOFREL could only profitably use half the 2,600 square metre site vacated by Thomson, GERIS sold the other half of the factory to ERAM, a medium-sized company that set up a warehouse employing 50 people.

The whole operation transferring the site to SOFREL and ERAM required considerable additional finance: FF24 million in all, over three years, even though Thomson sold both the buildings and machinery at advantageous terms. The finance needed was ultimately brought together from SOFREL, a group of private investors and additional loans from public regional authorities and state development funds.

The Thomson group was also involved in another case, that of SNEVAM. Facing severe competition, this time from eastern Europe, the group decided to restructure its production of certain electrical components, resulting in the drastic reduction of its workforce at its Nevers factory in January 1986. GERIS was again involved in this case in identifying an abundant local material, beechwood, which it considered could be the basis for a furniture factory. GERIS identified an Italian firm, DARON, which was prepared to set up a sawmill. A site was located with local assistance, about 25 km away, and finance of FF30 million was arranged from public and private sources. The sawmill started operating in 1988 with 60 workers and a chain factory was launched sometime later with a similar number of jobs.

Italy

ENI

Italy has also developed collaboration between large and small firms in a manner similar to the French experience. The case here regards the activities of the large ENI group, the major state-owned corporation engaged in the development and production of fuels, hydrocarbons and related products. In the early 1980s ENI was forced to move out of certain loss-making businesses and rationalize production leading to a substantial number of redundancies. ENI claims that apart from the other large public enterprise Montedison, it has been the only corporation in Italy which has helped generate replacement employment and business for its redundant personnel. The initiatives undertaken by ENI in the late 1980s included:

- Setting up two special companies, INDEMI and INSAR, in the mid-1980s to develop joint SME ventures of ENI and private partners to be taken over completely by the latter in due course. Some ten such ventures were started throughout Italy, creating around 1,000 jobs.
- The creation of small business substitution enterprises managed by cooperatives of former ENI workers. ENI assisted by guaranteeing the purchase of equipment and subcontracting agreements to cover the first years.
- Financial services provided by an ad hoc ENI organization (AGENI) to around 20 private companies in the textile garment sector on condition that 1,900 former workers from ENI companies would be offered employment.
- The supply of management services (together with local institutions) to companies formed by ex-ENI employees (or as joint ventures with ENI) as well as help with the creation of a technological industrial park in southern Italy.

ENI's experience has led the company to the conclusion that the role of a large enterprise in the area of underdevelopment or high unemployment or redundancies should be to initiate research and development in these regions to promote high-tech industries and to support a select number of local companies. This can be done through subcontracting and co-contracting agreements, providing technology transfer and helping with financing and developing market outlets. In this way ENI believes a partnership between large enterprises and SMEs is increasingly part of the large firm's role, and should be part of its production system.

Subcontracting

Throughout Europe, in countries such as France, Italy, Spain, United Kingdom and others, linkages between large and small industries industrial capacities have been fostered and promoted through instruments such as subcontracting exchanges, registers of potential suppliers and exhibitions where large firms display purchasing requirements and items they wish to purchase, as well as demonstrating the capabilities of SMEs to comply with these needs.

By the end of 1987, one year after an exchange (Borsa dell Subfornitura) was set up by Genoa Chamber of Commerce, a database of 500 firms from the mechanical, electronic and engineering sectors had been set up. The data included company organizational structures, market outlets, produce range and/or services, office and other relevant information such as turnover, number of employees, equipment and support staff and facilities. The Genoa Borsa has also been interested in cooperating with similar exchanges or initiatives in other regions of Italy and in other European countries. The Borsa achieved a significant expansion of subcontracting in the

Ligurian region (around Genoa) in part through cooperation between groups of small firms enabling the fulfilment of subcontracting orders beyond the means of a single enterprise. The Borsa has also attained a second objective in setting down conditions within the subcontracting agreements and defining more clearly the respective obligations of the partners.

The Borsa was created with the cooperation of DITGL (Ligurian Centre for Technology Diffusion) which has enabled it to offer a special quality-control service so that SME subcontractors can achieve a higher level of quality conformance and a range of technological improvements.

The Genoa Borsa is only one example of similar exchanges set up by chambers or other business associations elsewhere in Italy, in France (the first country to develop such exchanges in the 1960s), Spain as well as other European countries, and now also in several developing countries (India, Philippines, Latin America, Morocco, etc.).

East Germany

One of the biggest challenges in resolving labour and employment problems in the last decade has been in East Germany. The labour force of the former GDR stood at around 9 million, reduced by migration to the west to around 7.9 million by the end of 1991. Official unemployment was virtually non-existent in the GDR. It was statistically given as 19,000 at the start of 1990 or 0.2 per cent of the labour force but this increased to 1.34 million by January 1992 (17 per cent). This figure does not take account of 1.7 million (almost 20 per cent) part-time workers who were underemployed generally in specially contrived measures to control the transition "to a socially acceptable" level of displaced employees. A host of social measures was introduced — early retirement, short-time work, retraining and special employment promotion programmes — all intended to mitigate the social problems, financed by DM24 billion transferred by the Government to the eastern Länder in the two years 1991-92, for investment and job creation.

Treuhand and EPQCs

A major programme of industrial restructuring was undertaken (starting in late 1990) to accompany a series of privatization activities. A central holding company, the Treuhandanstalt, was set up which proceeded to transfer 9,000 companies from state to private ownership mainly through their rapid sale as complete entities to German or foreign investors. In the later stages of the process, after 1992, the sales involved some financial restructuring before transfer to the private sector.

The process managed by the Treuhand inevitably led to redundancies and employment shedding on a large scale. It was agreed therefore that active widespread measures were called for to make this conversion to a market economy "socially acceptable". To this aim various German social groups, employers' and workers' organizations, together with the Government and the Treuhand, joined forces to establish in East Germany "Beschäftigungsgesellschaft" (Employment Promotion and Qualification Companies, EPQCs). These companies were modelled on some earlier West German training programmes.

The 1992 Lichtenberger study for ILO (although at a relatively early stage after approximately two years' experience) raised some doubts as to whether EPQCs succeeded in raising skills to the required level and diversity or whether the operation of these companies really made the changes more "socially acceptable". Prior to the urgent social and economic problems thrown up by German unification, neither employers nor economists were supporters of such ideas on employment planning or special employment promotion companies. However, as an employment crisis developed in East Germany the former critics could find no viable alternatives and so began to regard the EPQCs as a potential solution to a difficult social situation.

The role of EPQCs as "employment promotion companies" involved at the time dealing with disagreements between employers and trade unions. The Treuhand strongly opposed any arrangement that extended employment within privatized companies and was concerned not to burden future buyers of the companies with further obligations. Finally, in late 1991, a compromise was reached whereby employees who were enrolled in an EPQC would legally be employed in that company and would sever their employment with their former employer.

By the end of 1991, there were 330 EPQCs in East Germany covering 130,000 employees. A further 90 were established during 1992, but after less than one year some EPQCs ceased operation.

The main role of the EPQCs is job creation. Although legal constraints in Germany do not permit direct conversion of such a job-creation scheme into a private enterprise, many such EPQC programmes have indirectly and unofficially "gone private within one or two years". In the early years of operation of the EPQCs there were accordingly no reliable statistics on the success of EPQCs in creating small enterprises. There is, however, a general statistic that between November 1989 and July 1991 the number of SMEs more than doubled, from 125,000 to 278,000 businesses.

Nearly half of the independent entrepreneurs existing in the GDR prior to November 1989 went out of business in this 20-month period. To equal the proportions in the former Federal Republic, there was a need to increase by five to six times the numbers in self-employment and small business in the East.

Reviewing the early experience of the EPQCs, Lichtenberger (1992) concludes that "they can provide a valuable means of minimizing the social consequences of economic restructuring. EPQCs with their employment-creation services and training schemes help remove obstacles to mobility and to solve problems of temporary unemployment". EPQCs, it is argued, can only be successful if there is close cooperation between employers and workers. With support from the private sector, employers, trade unions and regional institutions, East Germany's EPQCs did become instruments for regional policy and industrial restructuring by assuming some vital tasks in the deployment of displaced personnel. The limitations of EPQCs should also be recognized, even if there are no clear alternatives to the creation of institutions of this type.

The special role played by EPQCs, which might indicate their potential for replication in a similar situation in other countries, is best illustrated through an account of the tasks undertaken by a few companies of this type.

SAQ

The EPQC (SAQ) in Zwickau was founded on 3 July 1991 with a capital of $250,000. The only shareholder is the Sachsenring Automobile Co. Ltd., which succeeded the Trabant automobile manufacture after it was taken over by the Treuhand. SAQ started in October 1991 and continued with the ongoing employment-creation projects of the Sachsenring company. SAQ arranged employment creation as well as retraining and took care of short-time workers not involved in any programme.

The directors included a representative of the state of Saxony, the community of Zwickau, the Chamber of Commerce and Industry, the local Metalworkers' Union (IG Metall) and Volkswagen AG's training institution. SAQ is a leading member of the sectoral EPQC "Strassenfahrzeugbau Sachsen" (Saxon motor vehicle construction), formed at the beginning of this year from 38 car manufacturing companies.

The structural changes in the transition from a centrally planned to a market economy involved not only individual establishments but also entire economic sectors. The automobile industry of the former German Democratic Republic is an example where a whole sector was affected by the change to a market economy. The automobile industry was unable to compete against western markets. The headquarters of Trabant in Zwickau which employed 12,500 before the political change, closed down shortly after unification, and the Sachsenring operates as a supplier to the car industry and employed (by 1992) a total of 1,600.

In 1992, the SAQ had 338 employees in 15 employment-creation projects, with an average of 25 participants in each project. Only one project, the development and creation of a training and qualification centre, has more than 120 employees. Innovation projects, in particular, employ less than ten employees each.

The SAQ has an innovation department that carries out projects to analyse different techniques, processes and products to determine the possibility of using available buildings and amenities. The objective is to develop new product lines and services and to assess their marketability. The projects are intended to promote employment and to provide help and support in the establishment of new enterprises. Further technical training is provided.

Two centres were established for specialized workshops in metalwork, electrical engineering and wood processing, an EDP laboratory, as well as consultation and communication facilities. The project centres develop innovative building techniques, and methods of environmental protection which were backed by seminars, workshops of experts and which, it was hoped, would lead to the setting up of private enterprises. One example is the redevelopment of an "ecological building" project which employed more than ten project teams.

It was planned in the course of time to transform a number of the products and services identified as the basis of independent small firms with the guidance and help of the EPQC.

BeQua

A second EPQC was BeQua at Neuruppin, set up in May 1991 with 645 participants closely linked to the liquidation of EWP (Neuruppin) part of the former Kombinat Neuruppin (EPN), a major electrochemical corporation which, in 1989, employed 3,400 workers. After Treuhand's privatization of EPN, the workforce was reduced to 840. As many as 2,200 of the dismissed workers were given fixed-term contracts with the EPQC. They were engaged either on short-time work, detachments, special employment-creation projects or were offered retraining. Most of them were skilled employees.

Using public funds available, some of the employment-creation projects became independent small enterprises. This took place with the supportive intervention of other larger companies and employers' associations. Some team leaders developed into enterprise owners. The whole process of small enterprise creation through the EPQC initiative was slow and drawn-out as these skilled workers were unaccustomed to the option of self-employment and of owning their own business.

SAG Dessau

This was another EPQC founded in November 1990, one of the first such companies linked to the large Dessau Magnetbend Company (DMB), a major employer in the Dessau district. DMB was closed down in April 1991 and one of the leading managers of the research department then initiated an EPQC (SAG). DMB managers and SAG agreed on a contractual relationship which recognized the latter as a partner of DMB. Later another major employer in the vicinity, ELMO, made a large number of employees redundant and SAG began to employ their personnel too.

SAG's 814 employees (64 per cent of whom were skilled) were engaged in 40 different projects. These activities included "spin-offs" from former departments of DMB, such as catering services, and transport, which gradually offered similar services to the wider community. Not all the employees transferred to SAG performed satisfactorily and some had to be dropped from the programmes. In the first two years, 10 per cent of SAG's employment-creation projects were converted into formal SMEs, but there were many problems to be overcome: a lack of finance, premises, and a lack of business experience. By 1995, it was planned that SAG's employees would be reduced to 300, the rest having found employment. Public funding through the

Treuhand covered the costs of SAG as in the case of all EPQCs and there were some funds available to finance SME start-ups.

GEM

The fourth case was the EPQC set up in Brandenburg to deal with the huge retrenchment of labour at EKO Stahl, one of the major steel operations of the GDP which in 1989 employed 11,000 workers in the region which includes Eisenhattenstadt. After privatization, this was reduced in June 1991 to 3,200. An EPQC, GEM, was formed to take over 1,122 of the dismissed employees. GEM differed from some other EPQCs in that some of the employees actually returned to work in EKO, mostly on the rehabilitation of buildings and sites. GEM also set about helping create small enterprises, mostly services for the community: air traffic security, a farm restaurant, housing administration, crèche, travel firm, hotel school, etc. Most of the above were proposals for private businesses to take over what Eko Stahl previously provided as a public enterprise.

As in the other cases, GEM depended both on public funds made available by Treuhand and on the continued support of EKO Stahl. EKO was taken over in 1992 by Krupp Stahl of West Germany, who started reducing its support for GEM.

The EPQC's all found that there were few potential investors for its employment-creation projects except where the municipal and regional authorities were ready to invest to a limited extent in environmental protection and tourism.

Despite serious social and economic problems, the EPQCs did succeed to an extent both in retraining significant numbers of employees so that they could find work in the newly created and privatized restructured enterprises, as well as in helping develop self-employment and new SMEs. However, it should be recognized that such a programme to mitigate the social effects of a rapid transition to a market economy was possible only because of the enormous transfers of funds from West Germany.

3. The United States and Canada

In this chapter the focus is upon two elements of business-creation schemes that have not been covered in detail elsewhere: at one end of the employment scale, self-employment schemes for redundant workers, and at the other, employee stock ownership plans (ESOPs). The EDWAA job-creation demonstration is similar in many ways to the United Kingdom's Business Start-Up Scheme, and to similar schemes in other OECD countries;[1] however, the particular value of the study described here is what is revealed by the evaluation about the success of such schemes, and the income generated by self-employment. ESOPs are not, of course, business-creation schemes, however, they are one solution to the change of ownership following privatization, and they may be initiated specifically to prevent businesses being closed down and jobs lost. Even in companies not under threat, they may result in productivity increases and in new jobs.

The EDWAA Job-Creation Demonstration

EDWAA is the United States Economic Dislocation and Worker Adjustment Assistance Act which provides for retraining and re-employment services for workers who have lost their jobs due to retrenchments and closures. These people were typically defence employees or agricultural workers, but also included people made redundant from manufacturing and other industries.

In recent years, assistance with re-employment has been broadened to include a Job-Creation Demonstration aimed at providing entrepreneurial training to those people who wished to start their own business rather than seek re-employment. In 1991, the US Department of Labor (DOL) awarded grants to six community development organizations (CDCs) specializing in business start-up training to provide such assistance as an alternative to training for re-employment, and in 1993 an evaluation of this three-year demonstration was published.[2]

The evaluation examined the success of the Job-Creation Demonstration compared to the standard EDWAA re-employment programme, and by monitoring the participants of the programme was able to arrive at comparisons of business start-up rates compared to placement rates; business survival rates; number of jobs created and average income generated by the new businesses. Apart from providing useful feedback on the methods employed by the CDCs involved in the demonstration, it is fairly rare to come upon data of this type from any country on the outcomes of small business-creation schemes, and so the evaluation is useful from a more general perspective.

How the Job-Creation Demonstration was run

The CDCs undertaking the demonstration project used a variety of methods and operated in very different areas — some rural, some inner city. However, there was some convergence in the methods used during the three-year period. A degree of selection of the participants was found to be essential, in order to avoid large numbers of drop-outs during the programme. Participants were required to discuss their business ideas, and demonstrate some entrepreneurial qualities as well as sufficient financial resources for the business start-up before they were admitted to the programme.

Those who were admitted to the programme were generally better educated, rather more experienced and slightly older than their counterparts undergoing retraining for re-employment under the mainstream EDWAA programme, this difference probably being partly a result of the screening. It should be remembered, however, that efforts to increase the success of the

[1] Wilson and Adams (1994).

[2] Drury, et al. (1993).

programme in terms of high business start-up and survival rates inevitably led to a higher "deadweight effect", i.e. a greater proportion of people receiving assistance who would have been able to start a business without any help.

Participants were usually expected to attend classroom training over periods of ten to 13 weeks, and during this time they received help in preparing a business plan as well as individual technical assistance that continued during business start-up and the early months of operation.

Results from the Job-Creation Demonstration

Business start-up rates. The Job-Creation Demonstration was successful in promoting new businesses at least in the short term. Of the 645 participants of the six CDCs self-employment programmes, 45 per cent had started up businesses during the time-frame of the demonstration. Although this does not appear very high, it is comparable with start-up rates from other micro-enterprise programmes in Washington and Massachusetts (which ranged from 30 to 60 per cent). Also, many participants were successful in finding employment rather than starting their own business (29 per cent); and when the figures for self-employment and wage employment are taken together, 74 per cent compares well with the 67 per cent finding wage employment from mainstream EDWAA programmes. Clearly the job-creation programmes did not in all cases lead to new business creation, but it is probable that they improved the marketable skills of their participants.

Business survival rates. For businesses contacted six months after start-up, the survival rate was 74 per cent, and for the earlier cohort eligible for a 12-month follow-up, 76 per cent were still in business after one year.

Self-employment earnings. These findings were less encouraging. Many businesses did not operate full time, and even after 12 months of operation did not provide a living wage. Business earnings varied widely, averaging $1,193 per month for the six-month follow-up and $582 for the 12-month cohort, but in either case monthly earnings were considerably below the average monthly salary of mainstream EDWAA participants ($1,815 per month). Self-employment earnings were also lower than the average monthly salary that participants had enjoyed prior to being made redundant ($2,135).

Types of business. Service businesses were particularly prominent: although only 22 per cent of participants had been made redundant from this sector, 46 per cent started businesses in the service sector.

Recommendations from the evaluation

The attractions of small business-creation schemes are clear, anywhere in the world: they reduce the competition for available vacancies as well as diversifying local economies and fostering an entrepreneurial ethos. However, from the point of view of the participant, self-employment is a risky option, usually involving low earnings for the immediate future as well as the possibility of business failure. Unlike losing a job, the failure of a business venture often means the devastating loss of personal savings.

The evaluation recommended, among other measures intended to improve the quality of training and technical assistance of such programmes, that access to micro-loans should be improved for participants. Most participants had found it impossible to get loans for their business start-ups, and although some types of business did not require outside financing, others would have been severely limited by this. Lack of capital also restricts the type of business that can be embarked upon, leading to overcrowding and low survival rates.

Employee stock ownership plans

The philosophy behind employee stock ownership plans (ESOPs) is that if employees are enabled to buy shares in their own company, not only will they have a greater incentive to improve the productivity of the company, but they will have a greater control over the future of the company, especially when the current owners sell up. When the ownership of a company changes hands, the purchasers may only have been interested in the company's assets, and "restructuring" may be carried out with the intention not so much of improving the company's efficiency, but of closing down operations and laying off the entire workforce. ESOPs can be used to prevent such hostile take-overs.

How ESOPs are set up in the United States

Usually the company, and sometimes the employees and their union, decide to set up an ESOP trust to manage the ESOP. The ESOP uses the company's credit status to borrow funds on behalf of its employees. It uses this money to buy either new shares of the company stock or old shares from the existing owners (private or public). The ESOP then holds these shares "in trust" for the employees.

The company then repays the loan out of its profits. The loan repayments are treated as a payroll expense, like pension contributions, and so both the interest and the principal of the loan are deductible from taxable corporate income. As the loan is paid off, shares of the company's stock are allocated to each employee's account in the ESOP trust. In this way, employees gain shares in their company's stock, the company enjoys tax savings and both sides gain the benefit of an increased level of commitment on the part of the employees. When employees retire or leave the company, they can either take their stock with them, or sell them back to the company or in the market place.

How ESOPs have been used in the United States and Canada

Because of the tax advantages to the company of forming an ESOP trust, ESOPs have grown to an impressive number since their start in 1974. Approximately 12 million workers, or 10 per cent of the workforce, benefit from employee ownership in 11,000 ESOPs.[1] The main reasons given for starting ESOPs are to create an additional, popular employee benefit (about 40 per cent are set up for this purpose) and so that workers can buy their own company from departing owners (about 45 per cent). A small proportion of ESOPs have also been set up so that the workers can buy their own company during privatization, so that workers can prevent the firm being closed and jobs lost for economic reasons, and as a management defence against hostile take-over bids.

Benefits to the company. Companies tend to use ESOPs to reward their workers for loyalty, so it is no surprise that in those industries where a low turnover of skilled staff is more important — manufacturing and finance — there is a high proportion of ESOPs. Companies that have established ESOPs also find that they perform better, providing that as well as giving employees shares they also allow them to make an input into decision-making at all levels. It has been found that "ESOP firms in America grew 3 to 4 per cent per year faster than they would have without the ESOP, and that this growth created almost 50 per cent more jobs in the ESOP companies". Also, "most of the growth occurred in the most participative one-third of the companies — those that allow relatively high degrees of employee input into job-level decision-making".

Benefits to the employee. Surveys show ESOPs to be popular with employees; and the financial gains they represent are in some cases very significant. In terms of increasing worker

[1] Hansen (1993).

control, they have not yet grown to own a large share of productive capital in the United States (3 per cent in 1993); however, this proportion is likely to keep growing. Of particular interest to this study, however, is that, if ESOPs are combined with a participative management style, they can result in higher levels of productivity and more jobs.

There have been a number of cases in the United States of acting firms being bought out by employees to try and save their jobs. In the United States the record of troubled firms purchased by employees has been surprisingly good with only five failures recorded in 1986.[1]

An acting plant in Weirton, West Virginia bought by its employees in 1984 was regarded in the 1980s as one of the successes of the steel industry — the start of a series of mini steel plants. Consultants estimated a 32 per cent cut in labour costs would be needed, but later this was reduced to 18 per cent as output exceeded projected levels. Sales rose by 20 per cent and new investments have helped modernize the plant after the buy-out. According to Bradley and Gelb, Weirton also moved from a traditional management style to a more participative approach with support from both union and management.

Some general comments on buy-outs have been made. Small buy-outs tend to concentrate in areas of high unemployment, in isolated company towns where the cost of closure is high, both financially and socially. There is usually strong political pressure for public assistance and governments are more likely to intervene with support. The aim is to minimize job losses although practically all buy-outs involve substantial reductions in numbers of employees. In the United Kingdom some buy-outs have involved workforce reductions as high as 50 per cent,[2] while in the United States it has usually been around 30 per cent at the outset although in several cases there has been some increase in employment as business improved.

An interesting example is given in the case of a Canadian firm demonstrating the readiness of employees and management in a buy-out to reduce employment. During the prolonged negotiations on the buy-out, the workers were asked to estimate the minimum workforce they needed to run the business that previously employed 450. After some discussion they suggested around 130, but this proved too low and the plant finally employed 150.

There have also been significant productivity improvements with buy-outs. Particularly after MBOs, there are less quality rejects and less material waste. The Canadian firm mentioned above was able to reduce quality control personnel from 57 to 10 without increasing the number of defective products. However, it should be remembered the main aim of buy-outs, in the vast majority of cases, is to save jobs resulting from plant closure. If plants raise product quality and productivity there are prospects of employment creation in the future.

[1] Bradley and Gelb (1986).

[2] ibid.

4. Central and Eastern Europe and the former Soviet Union

Introduction

The major industries in this region have suffered from sharp output declines as the transition to a market economy gathered pace. Major restructuring of industries is taking place with privatization, but unlike the process in the rest of Europe where restructuring has been going on for almost 20 years, it is being carried out at speed over a short period.

The growth of micro-enterprises

As a result of the changes legalizing private sector activity in most countries in the region around 1990, most of the economies in the region now have huge numbers of private small businesses and micro-enterprises.[1] However, many of the jobs are in the informal sector, simply providing some additional income to boost low-paid state-sector employment, or allowing employers to take advantage of tax breaks. Micro-enterprises, rather than SMEs, comprise the vast majority of private businesses; in Hungary, for example, 96 per cent of businesses have under 11 employees. Self-employment has been seen by governments as one way to reduce the sharp rises in unemployment experienced for the first time in this region, and the schemes of Poland and Hungary are two examples described here.

The relative absence of rather larger SMEs is regarded with concern, however, partly because of their greater potential for providing employment, and also largely because of the need to transfer economic control in these countries from the hands of the few to the many. There is an urgent need to establish business support and financial infrastructure to help some of the business start-ups of the early 1990s grow larger. There is also great potential for the restructuring of large, formerly state-owned industries to produce many smaller units, through spin-offs, and management buy-outs, with a smaller amount of job-shedding (see the examples given in the sections on Romania and the Russian Federation).

Post-privatization business support

The emphasis among the agencies who are involved in restructuring has often been upon identifying how to salvage some part of an ailing large state-owned firm to turn it around to profitability, and if this involves large sections of the firm being made redundant then this is a necessary problem that must be dealt with by other agencies or schemes (an exception being the work on spin-offs undertaken in Romania). The presence of a thriving small business sector, however, has in some countries lessened the opposition within large industries to restructuring (see the section on the Czech Republic), so small business support is an important plank in the overall restructuring process.

Major investment by the restructuring industry in small business promotion schemes, such as those run by British Coal Enterprise and British Steel Investment, do not appear to have been attempted. Presumably a lack of financial resources, as well as the time to build up the necessary experience in investing in successful new businesses while the restructuring is taking place, have both mitigated against this.

There are many donors, however, who are currently running programmes of business support, including business advice and consultancy, venture capital investment, credit guarantee schemes for small businesses and workspace provision, and who are above all aiming to transfer

[1] Charap (1992).

the skills to local counterparts and support local institutions with the capability to run such programmes.

Finally, it should be noted that, especially in the former Soviet Union, large enterprises that are now being considered for restructuring and privatization were far more than places of work for their employees: they often provided housing, medical facilities, leisure and holiday benefits, as well as pensions. It is hardly surprising that, in the absence of a well-developed alternative state provision of these benefits, many managers as well as their employees are reluctant to embark on restructuring that will lead to redundancies.

Poland

Throughout the communist era, some private sector activity was allowed and regulated in Poland. In 1989 the "Law on Economic Activity" was passed, bringing reforms to the private sector, and by the end of the year 16,000 sole proprietorships and more than 16,000 new companies were registered.[1]

Poland's Ministry of Labour and Social Policy (MOLSP) has run its own self-employment scheme for the unemployed, equivalent to the United Kingdom's Business Start-Up Scheme, and this will be described later. For the most part, donor organizations who have played a part in Poland's restructuring process have concentrated on the SME, or growth-orientated small business sector, rather than the self-employed.

Two schemes have been funded by the European Commission's PHARE programme: the Small and Medium Enterprises Sector Import and Support Programme (ECU6 million, or $6.6 million) and the Private Sector Development Programme (ECU6 million). The Structural Development in Selected Regions (STRUDER) programme, also supported by the PHARE programme (ECU76 million), was designed to aid SMEs and to contribute to local infrastructure and training. STRUDER is implemented by the Polish Agency for Regional Development.

Following on from the work of STRUDER, the Polish-British Enterprise Project (PBEP) is a joint initiative of the Polish and British Governments to provide assistance for SMEs, in particular in the regions of Lublin and Bialystok in eastern Poland. PBEP is a five-year project which was started in 1995 with $19 million; it is the largest programme sponsored by the British Know-How Fund in Central Europe. The four main components of the project are: a business development programme; an equity investment fund for SMEs; a credit guarantee scheme and a market development programme.

Business support infrastructure

Around 1989-90 no institutional structures to support small businesses existed, so it is remarkable that by 1993, largely with the help of donor funding, the following numbers and types of organization were in operation:[2]

- 123 regional development agencies and foundations. These were set up in areas facing particular structural unemployment, and they coordinate restructuring plans with SME development programmes; promote the activities of local business support agencies such as those belonging to the Foundation for Social and Economic Initiatives, FISE; establish investment funds including equity, loans and guarantees; and promote Polish businesses on foreign markets;
- 52 innovation and entrepreneurship centres. These include business incubators designed to provide training, advice and office support facilities for new businesses;

[1] Webster (1992).

[2] Hubner (1996).

- 314 chambers of commerce and business associations. These are an important channel for bringing SME issues to the attention of the government; they also provide their members with advisory services, training courses, business contacts, and so on;
- 112 advisory, information and training institutions, devoted to providing these services to businesses of all sizes;
- 72 promotion and trade institutions, established with the economics departments of regional offices to promote businesses both locally and abroad. Among other activities they organize trade fairs and auctions.

In the initial stages, basic services for business start-ups were provided; however, many businesses now require more in-depth consulting services, and the institutions are beginning to adjust to this. In 1995, the Polish Foundation for the Promotion and Development of Small and Medium Enterprises was established by the Polish Government to be the responsible agency for work within the sector. Its mandate is to communicate to SMEs, to implement policy and to guide and coordinate existing support activities. The Foundation has a council with representatives from the key institutions in the public and private sectors, and a staff of professionals who have already been involved in implementing and evaluating SME support through the two PHARE programmes.

Finance for SMEs

A lack of finance is seen as a major constraint for small businesses in Poland. Banks are unused and unwilling to lend to this sector, which is one reason why micro-enterprises find it hard to expand into small and medium businesses. Several credit guarantee schemes have been set up in Poland to reduce the exposure to risk of banks lending to small businesses. A comparison of various credit guarantee schemes, as well as an equity investment scheme and a business grant scheme is given in table 3.

Table 3. Finance for SMEs in Poland

	BGK[1]	PHARE[2]	PBEP loan guarantee fund	PBEP equity investment fund	STRUDER PARD (grant)
Amount in fund	$18 million	$3.07 million so far guaranteed	$4 million	-	$7.9 million
Size of investment	-	$18 720 (average)	$5 000-$52 000	$10 000-$150 000	$125 000 maximum
Term of loan	1-5 years	-	Up to 5 years	4-7 years	-
Starting date of fund	Apr. 1995	-	Jan. 1995	Jan. 1995	Apr. 1994
No. of investments made by date	0 (Mar. 1996)	164 (Feb. 1996)	60 (Sep. 1996) through eight banks	2 (Sep. 1996)	200 (Apr. 1995)

[1] BGK is Bank Gospodarstwa Krahowego.
[2] These figures include eight local guarantee funds capitalized by PHARE.

Source: *Small Enterprise Development,* Vol. 8, No. 2; Polish-British Enterprise Project (1996), *General information;* Kozak (1996): *Small business in transition economies* in Levitksy, J. (ed.), ITP, London.

The loan guarantee fund operating through the state-owned bank BGK (Bank Gospodarstwa Krahowego) was funded by Poland's Ministry of Finance, and is intended to cover loans made by 12 banks who have signed cooperating agreements. PHARE has funded eight local guarantee funds which were placed with local development agencies. The STRUDER fund operated by PARD (Polish Agency for Regional Development) is an unusual scheme offering a grant to small businesses for up to 25 per cent of their investment, the rest being raised either from own funds or from a bank loan. A guarantee scheme is available for loans to cover 55 per cent of the remainder of the investment. This is a substantial guarantee fund of $7.9 million; however, no guarantees had been made by mid-1996.

The Polish-British Enterprise Project's Equity Investment Fund is aimed at providing SMEs with medium- and long-term venture capital. Up to the end of 1995 EIF had presented its offer to 200 clients and received 50 inquiries; it was analysing the applications of 20 firms. By October 1996, PBEP's Equity Investment Fund had made two investments.

What is apparent from table 3 is that in spite of the demand for institutional finance, the number of investments made are still very low. By early 1996, no loan guarantees had been made from the BGK fund, nor from the PARD scheme. In the case of credit guarantee schemes, it sometimes takes a number of years before sufficient trust develops between the banks and the guarantor for the banks to take advantage of the scheme; before this time banks are often doubtful about the reliability of the claims procedure. Once credit guarantee schemes are well established, however, a given amount in the fund can be expected to leverage up to five times its value in guaranteed loans. For this reason, and given time, credit guarantee funds can be a cost-effective way to assisting banks to lend to SMEs.

Similarly, it takes time for the managers of equity investment funds, such as that run by PBEP, to develop experience in identifying suitable businesses with growth potential. To select only two businesses for funding after analysing 20 applications at the end of 18 months is by no means unusual: in fact most commercial venture capital companies expect to invest in between 2 and 10 per cent of the businesses they analyse. Commercial investors of equity funds would normally look for an internal rate of return on their investment of at least 25 per cent per annum, and although funds aimed at SME development can settle for less (18 per cent is given by one such programme),[1] much lower rates would result in the depletion of the fund. However, in view of the need for long-term investments, particularly for financing management buy-outs or spin-off ventures, the present low impact of equity investment funds, should be regarded with patience. It is no coincidence that the second largest market for MBOs is in the United Kingdom, which has the largest venture capital investor in Europe, 3I.

Schemes for self-employment

In common with most western European countries, Poland's Ministry of Labour and Social Policy (MOLSP) operated in 1992 a scheme aimed at encouraging unemployed people to move into self-employment. The PNIDZ programme, loans for individual economic activity, was aimed at individuals who were either unemployed or had received notice by their employers of an impending lay-off.[2] The scheme took into account the difficulty experienced in Poland by such people in obtaining start-up capital, and rather than providing a regular allowance as in other countries, it offered a lump-sum loan at the start of the programme.

In view of this attractive sum, participants in the scheme were obliged to undergo a certain amount of screening. First, they were interviewed by a local labour office representative, who would only issue an application form if the interviewee answered his questions about the nature of the proposed enterprise satisfactorily. The application form asked further questions about the nature of the enterprise, the financial plan, and the size of the loan requested; and the completed form was appraised by the Local Labour Councils. Those passing this screening stage were then

[1] Gibson (1996).

[2] This section is based on Wilson and Adams (1994).

obliged to attend a period of business training undertaken by a contracted business advisory organization. The quality of such service providers often varied, particularly in the regions where these services have only recently become established.

Further capacity problems arose relating to the disbursement and monitoring of the loans, which were released to applicants once they had successfully completed their training, and MOLSP in 1992 was beginning to transfer these functions to private sector organizations specializing in business advice and training.

The business loan itself had the following features: it is a maximum of 54 million zloty (US$4,000), which is as much as 20 times the average monthly salary, with a maximum term of four years. No collateral was required, though two guarantors were required, and the interest rate was subsidized. One feature helped to increase the payback rates: borrowers who kept up with their instalments for the first 24 months could ask to have the remaining 50 per cent of the loan waived. Some offices reported payback rates of 90 per cent; in other regions it was 60-70 per cent.

This loan scheme made the PNIDZ programme relatively generous compared to similar schemes in other OECD countries, and compared to unemployment benefit (the amount of the loan was on average three times greater than the benefits which would be paid for the period). The justification for this was that there are few alternative sources of start-up funding for the unemployed in Poland. Interestingly, in spite of the attractiveness of the loan sum, even when participation in the PNIDZ programme has been at its highest, under 3 per cent of the unemployed have opted to join the scheme. This may be attributed to the screening process which loan applicants have to undergo.

Very little information is available on business survival rates or numbers of jobs created for participants of the PNIDZ programme, compared to similar programmes in OECD countries. Some points may be made concerning participation levels, however. The PNIDZ programme was funded, along with other employment assistance measures, from the Labour Fund, the main part of which is directed towards paying unemployment benefits. In 1991, unemployment was low and the PNIDZ programme received almost 14 per cent of the budget, with 32,000 participants being funded. By 1993, however, unemployment had risen sharply and benefits to the unemployed were crowding out the PNIDZ programme's share of the Labour Fund's budget, which dropped to 1 per cent. This budgetary constraint on a self-employment scheme might have been reduced if the PNIDZ programme had been transferred out of the Labour Fund.

Hungary

Private sector activities had been permitted in Hungary since the 1960s, but it was in 1989 that the Act on Economic Associations created the legal framework for operating commercial enterprises. In 1990 the Hungarian Foundation for Enterprise Promotion (HFEP) was launched by the Hungarian Government, with the support of eight major commercial banks and of the country's main business associations.

HFEP operates through a network of independent local enterprise agencies (LEAs) which by now covers the whole country, providing business advice and information, training programmes, managed workspace and financial assistance. The centrality of HFEP's coordinating role is demonstrated by the fact that the Foundation and its networks receive support from 12 different bilateral donors, as well as the European Commission's PHARE programme.

Credit for SMEs

In Hungary, the banks' normal reluctance to lend to this sector is coupled with collateral requirements for SME loans of, typically, 100 per cent of the capital of the loan plus the interest and often 300 per cent of the value of the loan for enterprises thought to be "risky". Loan guarantee schemes have been introduced to reduce the risk element as perceived by the banks.

The preferential credit schemes aimed at SMEs are:

- existence credit scheme (aimed at promoting privatization);
- microcredit (loans of up to $2,300, administered by the Hungarian Foundation for Enterprise Promotion from PHARE resources, and aimed at new and existing businesses);
- PHARE loans of up to $80,000 for terms of up to seven years;
- start credit (aimed at start-ups and administered by the Hungarian Foundation for Enterprise Promotion from German Government resources, and relying on a special credit guarantee scheme);
- reorg START (enabling SMEs to buy up the properties of bankrupt companies; loans are up to $120,000); and
- Japanese credit (financed by the Japanese Eximbank, and aimed at start-ups).[1]

ESOPs in Hungary

It is clear that there is at least one credit scheme aimed at enabling SMEs to buy and restructure existing companies: this reflects the level of institutional support for changes in ownership in Hungary. Among eastern European countries, Hungary has the most advanced ESOP legislation, which allows employees to become shareholders through special organizations, similar to American ESOP trusts. Out of approximately 1,800 state-owned enterprises which were in the process of being privatized in 1994, 150 had been sold to ESOPs, and 70 had chosen a combination of ESOP and MBO, with a further 30 ESOPs and 70 ESOP plus MBOs in the process of being established.[2] Enabling workers and managers to buy shares in their old companies on the one hand increases economic democracy and on the other provides managers with incentives for making the newly privatized companies grow.

Self-employment schemes for the unemployed

In 1989 the Ministry of Labour introduced a credit programme aimed at unemployed people who wished to become self-employed.[3] The Restart Loan for Unemployed and School Leavers (known as the UJK scheme) was discontinued after two years because of poor performance and was replaced by the Unemployment Benefit Programme for Entrepreneurs (MVVE scheme). In 1994, this second scheme was not performing well either; in both cases the trouble seemed to lie with the fact that although the benefits of the programme relative to alternative unemployment assistance were considerable, the programmes were not screening clients effectively.

In 1990 the original target group was widened to include all the unemployed, however short or long their period of unemployment. UJK participants had to apply to a local labour office, where they were referred to a bank, to whom they submitted a business proposal. They were expected to supply collateral or a guarantor for the loan. They also had to obtain an "entrepreneur card", which was easily acquired by registering the business with the local authorities. When the MVVE scheme replaced this programme, even less screening was undertaken, since banks were no longer involved and applicants were not expected to supply a detailed business proposal or to attend training. Neither scheme required applicants to be

[1] Futo (1997) and "Hungarian Foundation for Enterprise Promotion", notes and news item in *Small Enterprise Development,* Vol. 6, No. 4.

[2] Hansen (1994).

[3] This section is based on Wilson and Adams (1994).

questioned about their business plans, and the screening was much less effective than any other OECD country, or even Poland.

The benefits of the UJK programme were: a loan of $6,000 (in 1990) of which the interest was paid by the Ministry of Labour. Given the attractiveness of the scheme, it is not surprising that in 1989 almost half the unemployed joined the scheme, falling to 37 per cent in 1990. The costs of the interest payments being paid by the Ministry of Labour were considerable, and as a result the more modest MVVE programme was introduced: six months of a monthly allowance plus a 50 per cent cost rebate on business advisory services. Even so, the number of participants continued to rise. Very few of the MVVE participants took advantage of the subsidized business counselling, which would suggest that many of them were not serious about entering self-employment. The number of participants on these schemes was a much larger proportion of the unemployed than would usually opt to join similar schemes elsewhere (rarely over 5 per cent in most OECD countries); and can be attributed to the lack of screening of applicants.

The Czech Republic

Opportunities for new enterprises during the privatization process

In the Czech Republic the problems of soaring unemployment, and of how to find jobs or self-employment for retrenched workers, have been relatively minor. Unemployment has remained very low during the privatization process, at least until 1995 (it has rarely been over 4 per cent, and is one of the lowest in Europe);[1] so it is interesting to examine the characteristics of the privatization process to see how opportunities for employment have developed. Here privatization has taken place in different stages, beginning with the restitution of property to its former owners (or their heirs) and the sale of small units to prospective entrepreneurs. This in effect gave a kick-start to the growth of a small private business sector immediately after the velvet revolution in November 1989 and, by 1995, 600,000 jobs had been created in the small business sector, representing about one-quarter of total employment.

The privatization of large industries in the Czech Republic took place in the early 1990s through direct sale, auction or voucher privatization. About half of the companies were sold to the private sector as single units before any restructuring had taken place, and then the new management had the responsibility of deciding which parts of the operation could be kept and developed, and which units would have to be abandoned, and their workers redeployed or made redundant. In the rest of the cases, managers of state industries had the opportunity to reorganize the firm, making at least some units look attractive to private buyers, before privatization of the separate units took place. Managers were in a position to choose how various parts of the firm could be sold off, and to try to acquire sections of the firm; alternatively they could maximize the chances of being kept on as the manager themselves, without getting a share in the property. Many managers who wanted to get a stake in the company opted to make redundancies among unskilled or clerical workers, while keeping on their experienced technicians to form a core team.

Sometimes large numbers of workers were made redundant, and received severance pay; however, many workers decided to leave the firm voluntarily and seek alternative employment when they knew that privatization was planned. The advantage of the second option was that those who left early on had a better chance of gaining employment in one of the new growth businesses that were emerging. Those who waited until privatization had taken place and received their redundancy payments (which obliged them to remain out of work for five months) found themselves some way down the queue for the best jobs.

[1] Paukert; Liba (1995).

Many workers chose to leave their public sector jobs to start their own business. In fact, many people started their businesses while still in employment, and only left their full-time jobs when they judged their new businesses were strong enough to survive. Surveys by the ILO confirm this finding: more businesses were started up by workers leaving their state sector jobs voluntarily than by people who were already unemployed.

Although the Government had intended the privatizations to take place speedily, in many cases the need for flexible solutions to the problems that arose slowed down the progress considerably. This had some advantages for both workers and managers: managers had time to work out how to restructure the industry to enable at least some parts to be attractive for workers and management to buy a share. In addition, workers who could see no future for themselves in the parent company had time either to find a suitable job elsewhere or to get their own business started before they were forced to leave.

Romania

The advantages of taking time to solve the problems of restructuring during the privatization process are also demonstrated in the work on spin-offs in Romania. This project was undertaken by the Durham University Business School (DUBS) Small Business Centre in partnership with the Romanian Institute of Management (IROMA), with the support of the British Know-How Fund from 1994 to 1997. It deals specifically with helping large businesses in the process of restructuring to identify separate profit centres that have the potential to be "spun-off" as separate businesses. While the situation in Romania may be different from the rest of Central and Eastern Europe and the former Soviet Union, all of them at different stages in the transition to market economies, the processes through which managers of the industries passed are generally applicable, and useful outside this region. However, the case-studies of spin-offs alluded to here[1] present a variety of problems that the managers had to deal with, illustrating that the only universal was that they had to possess flexibility and the confidence to carry through their proposed plans.

The context

As in the rest of the region, Romania is engaged in the process of its large, state-owned firms undergoing widespread restructuring and privatization, while at the same time attempts are being made to develop private sector small and medium businesses. Because of the loss of their Eastern European and Soviet markets, the capacity of many firms is under-used, and there is no immediate prospect of returning to earlier production levels. Unless such firms are able to lose some of their excess capacity and under-used workforce, they will never become efficient; however, the process of streamlining is a difficult one to carry through, and one which most managers are unprepared for from their earlier experience within a centrally managed State.

The joint project between DUBS and IROMA started with two training programmes, the first one for senior managers intended to persuade them of the benefits of forming spin-offs, and to help them to identify and write a proposal for a possible spin-off within their own companies. The potential advantages of starting a spin-off are that it could remove from the parent firm excess assets, workforce and overheads; and as a separate entity the new firm could continue to supply the parent firm on a commercial basis as well as seeking new clients. Once a business proposal had been conceived by the senior manager, a potential spin-off manager would be nominated, and it would be this manager who would attend the second training programme, the "new venture programme", consisting of three one-week workshops at monthly intervals. During

[1] This material is based on Nelson and Taylor (1995).

this time the new venture manager would formulate a business plan. As the spun-off firm began its existence, assistance and support would be provided to help it survive the early years.

The firms that have undergone this training and help with restructuring number approximately 250. Several case-studies are given in Annex 1, illustrating how varied are the problems faced, and the solutions which are emerging.[1] No single formula can be offered for spin-offs, and the management problems that arise are continual, requiring strategic decisions across largely uncharted territory.

The difference between the situation in Romania and the United Kingdom, for example, is that the privatization process has been happening in the United Kingdom for almost two decades, allowing spin-offs to evolve gradually, within a fully functioning market economy; in Romania the situation is one of often "sick" businesses being privatized, within a short space of time, in an economic climate that is far from supportive. The case for experienced management consultancy in this situation is very strong.

Russian Federation

Access to finance is a major problem for large or small businesses springing up in the wake of major privatization and retrenchments in the former Soviet Union. In some regions of the CIS, such as the Central Asian Republics, the banks are held in such poor public regard that not only do they not have the funds or capability to lend to small businesses, but they have difficulties financing large ventures. In contrast to this, the European Bank for Reconstruction and Development (EBRD) has had some success in involving a number of banks in the Russian Federation in lending to SMEs.

EBRD's Russia Small Business Fund

The EBRD has been running the Russia Small Business Fund (RSBF) since March 1994, with the aim of financing micro-enterprises and small businesses which generally do not have access to formal sector finance, and also of building the capability of the local banking system to continue to lend to this target group on a sustainable basis, once the programme is over. The programme was set up with $150 million in promised funding from the G7 countries plus Switzerland and $150 million of the EBRD's resources.

There are two main products. Microcredit consists of loans up to $20,000 (exceptionally to $30,000; the average loan size is $5,000), and is intended for businesses from all sectors. The second category is small loans, with an average size of $50,000, although they can be as much as $125,000. These loans are restricted to the production and service sectors only, and they are generally for longer-term investment. Since the start of the programme, 10,000 loans have been disbursed for slightly over $100 million. Monthly disbursements are presently $9 million, and they are expected to reach $20 million by the end of 1997.

The RSBF began its operations with banks in Nizhny Novgorod, Tula and Tomsk, and now operates with 12 Russian commercial banks in a number of cities and small towns. Tula is a city formerly dominated by the armaments industry, and surrounded by coalmining towns; many redundancies have been made during the process of restructuring these industries, making it now a considerably depressed region. Tomsk was similarly dominated by a military research establishment which has now been closed. The RSBF has moved beyond these cities now, and includes some relatively prosperous areas such as Moscow, but in most areas the effects of restructuring have been felt, and support for small businesses capable of providing new employment is important.

[1] These case-studies are taken from Nelson, et al. (1997).

Indicators of success. Data on the businesses themselves have not been assembled; however, information on default rates at least indicates whether the businesses have been healthy enough to repay their loans. This information is encouraging: default rates are low and many SME borrowers are expanding and returning to the banks for subsequent loans. The banks are achieving arrears on programme loans typically of up to 3 per cent and losses to end 1996 have been less than 0.5 per cent on disbursements to final borrowers of around $100 million. Because of low losses and reasonable margins, the more active banks in the programme are reaching break-even and profit in the first year. The programme in some branches not only covers its own costs, but the entire operations of the branch. This should be encouraging for banks considering whether to expand their lending to this target group, independently of donor funding.

The EBRD lays great emphasis on its relationship with the partner bank and upon helping to build its technical and institutional capacity. The key to micro-lending is an efficient credit technology, and a swift and unbureaucratic credit extension process. Once these processes have been adopted, the banks concerned are able to reach a new target group and diversify their own portfolios, thereby contributing to a healthy banking sector.

Spin-offs — The case of Prompribor

As in Central and Eastern Europe, the transition to a healthy market economy in the Russian Federation is hampered by the "missing middle" of small to medium enterprises. A case is made for creating small businesses out of large enterprises by Allan Gibb and Stanislav Lyapunov in their article citing the example of the state company Prompribor (of which Lyapunov is the Chairman of the Director's Board) in the Russian republic of Chuvash.[1] Some of the problems in creating spin-offs in the Russian Federation relate to access to resources: with little hope of gaining bank finance, any spun-off small business is bound to be dependent on the core enterprise for capital as well as for contracts. It is also important to ensure that new managers can gain incentives in the form of ownership or shareholding.

In 1989, Prompribor was a large state-owned company employing 3,000 workers, having as its core business electrical actuators and electronic devices, but also including activities as diverse as the manufacture of tools, packaging, and maintenance equipment for the building industry. The chief executive wanted to manage the privatization process in such a way as to generate more work for the 30 per cent of the workforce deemed to be excess labour, and he chose to establish spin-offs to do this.

The various ownership options for the new businesses were: a completely independent company, bought out by the workforce; an independent company with the state company as a minority shareholder; an "independent" company, but with the state company as a majority shareholder; a subsidiary of a state company, but with a high degree of autonomy; and a complete subsidiary with limited independence. The variations that included a greater level of ownership by the managers and workforce were preferred, since this would increase their sense of responsibility for the new ventures; however, a lack of personal wealth or access to institutional finance made this difficult.

Eventually, as a number of potential spin-offs were identified, and their managers selected and trained, a solution was found to the financing by turning the core business into a holding company. At the start of each new spin-off, the core business took up 99 per cent of the shares and the manager was given 1 per cent. Then, after 18 months, the share of the manager and workforce was raised to 10 per cent, and gradually, by reinvesting the profits and borrowing from friends and outside investors, the private ownership of the new venture was increased. By August 1994, the Prompribor Association consisted of 25 linked companies, with the holding company owning between 3 and 95 per cent of the capital of these companies. Many of the

[1] Gibb and Lyapunov (1995).

smaller companies had expanded and were operating autonomously, and at this point in the restructuring process only 200 jobs had been lost.

The experience of Prompribor is not unique: during 1993 and the first four months of 1994, as many as 12,000 companies were sold through the voucher programme, giving their employees the opportunity to buy shares in their own workplace. Outside the Russian Federation, DUBS is working in Romania, also funded by the British Know-How Fund, as a direct follow-on from this project. However, Gibb and Lyapunov identify several factors that helped to make Prompribor particularly successful in terms of launching new businesses and retaining jobs. The vision and determination of the chief executive were essential in leading the company through such uncharted territory, and it was particularly important that the restructuring process had begun *before* privatization took place, since this gave time for the many decisions to be made regarding the new companies and their relationship with the core company.

If managers are to be assisted with this process then the emphasis should be upon "teaching managers how to: review the structure of their businesses; make decisions on what needs to be pruned and disaggregated; discover what are the main actions that need to be taken to do this; decide what skills, attitudes and motivations will be needed to manage this and how they themselves might develop suitable programmes and activities to meet these purposes". [1]

[1] ibid.

5. Corporate support for SMMEs in the Republic of South Africa

As might be expected from the long, dark history of the oppressive apartheid system, the Republic of South Africa (RSA) has suffered for many years from large disadvantaged groups, deprived of employment and opportunities of participating in business development. Accordingly, it is not surprising that even before the collapse of the apartheid system, some large corporations had already promoted initiatives to support SMME (small, medium and micro-enterprise) development and especially in helping establish black-owned businesses.

The Anglo-American Corporation (AAC), the largest corporation in the RSA, was the first to launch such an initiative in the mid-1980s, and now has the largest small business support programme of any corporation in the country. AAC's programme started by helping small, mainly black-owned businesses through a programme of "outsourcing" a large portion of the corporation's purchases from such small firms. For some time those engaged in small business promotion in the RSA have sought to convince such very large white-owned corporations that purchasing inputs from SMEs and developing subcontracting operations involving small — including black-owned — businesses also makes good sense from an economic and business perspective and that, over time, the commercial and indirect benefits will exceed the costs incurred.

This could be the strongest argument to persuade some hesitant managements to develop a small business unit (SBU). However, even though, understandably, there may be a reluctance in making small business support appear as a form of philanthropy or as a way of placating politicians who are pressing for affirmative action, the situation of several corporations who operate as the main source of employment and wealth particularly in smaller towns in the RSA, imposes a duty on these companies to the community from which it draws a great deal of its resources to help develop and sustain local businesses.

A thriving small business sector in a town where a corporation operates, helps to stabilize the workforce to mitigate the corrosive effects of unemployment and idleness, as well as ultimately enhancing the corporate image and the commercial performance of the larger firm. Some shareholders and managers may dismiss investments or other costly support efforts by a corporation to stimulate and strengthen small businesses in the locality which do not produce direct commercial returns (new suppliers, savings in procurement, more specialized subcontractors, etc.) as unnecessary expenditure. However, most large corporations in the RSA now recognize that "social investment" to help the disadvantaged in local communities to start and develop small businesses is not only good public relations but will in the end produce indirect returns in the long term in the benefits (mentioned above) accruing from a close cooperative relationship with the local business sector.

So far (to 1996) only some of the larger, more far-sighted, corporations in the RSA have developed comprehensive SMME support programmes and, as stated, even among these some are focused almost exclusively on developing new suppliers and subcontractors. However, in the the RSA as in other industrialized countries, a number of other far-reaching initiatives have been developed by the corporate sector.

- Corporations have helped micro-businesses and SMEs to process further, or distribute its products (downstream linkages) e.g. some textile cloth or footwear manufacturers have developed clothing production and retail outlets.
- Together with other large enterprises, forming groups for corporate support for SMEs to set up "one-step" assistance centres within localities to provide advice and assistance to small-scale businessmen and women on such matters as: how to obtain premises, marketing help, technological, legal and fiscal advice, obtaining materials at lowest prices, where to

find suitable courses to help improve management, etc. (along the line of the enterprise agencies in the United Kingdom).

- Working with SBDC (Small Business Development Corporation — see below) on developing small estates (hives) or incubators for local businesses, and in finding suitable participants for SBDC training activities.
- Seconding staff (whole and part-time) to offer central services in incubators/hives, advisory centres and consultancy assistance for small businesses.
- Helping set up small venture capital funds (e.g. AAC's LITET — see below) in promoting equity investments in SMEs and help in disseminating information on these schemes to facilitate their use by suitable entrepreneurs.
- Increasing subcontracting relationships through the organization of local subcontracting exchanges, arranging registers, databases and exhibitions to help generate more demand for subcontracting. This helps match available capacity and capability to meet requirements for quantity, quality and delivery of items or services.
- Offering assistance to small businesses in obtaining loans, finance (and/or guarantees) through Khula (see below) and through the banking system.

Small Business Development Corporation (SBDC)

SBDC was established in 1983, and for the first years of its operation appeared to be managed in accordance with the policies of apartheid. However, in the past few years, especially since 1994, SBDC has undergone a drastic restructuring as regards its ownership, management and role. It is now clearly a private sector corporation with government participation reduced to 30 per cent (previously 50 per cent) with the remaining 70 per cent held by private sector corporations (from 1 or 2 per cent shareholding to 20 per cent in the maximum case).

Under the agreed changed role, SBDC has transferred its credit and guaranteed loan portfolios to the newly created government-owned Khula Enterprise Finance Limited which is to become the main SME financing organization working with the banking system and providing, where needed, loan guarantees to the lending banks. SBDC now offers investment capital and what is called "value adding business support" to viable SMEs, especially black-owned businesses. The financial packages of SBDCs will provide between R50,000 and R3 million at market rates and will take equity positions where justified in place of security.

SBDC also has among its assets 43 industrial estates and 12 informal "hives" (small estates for micro-enterprises) housing 3,500 small businesses in all. It is intended that this valuable property will, in different ways, be sold off in due course to the private sector.

It is generally accepted that SBDC has, without doubt, the most comprehensive database of small business suppliers in RSA. Helped by AAC with seed capital of R250,000, SBDC launched a small business subcontracting initiative in 1989, particularly focused on the subcontracting potential of the SMEs located in the industrial estates and "hives". Clearly the database needs updating to include new black-owned businesses that have sprung up in the last few years, and this is being done.

Public and private small business initiatives

As mentioned previously, Anglo-American (AAC), the largest corporation in RSA, started a small business initiative in the mid-1980s, which provided services to small black-owned businesses which, in turn, supplied goods worth over R40 million (US$8.9 million) to AAC in 1995. AAC has created a small-business venture-capital fund, LITET (Labour-Intensive Industries Trust Ltd.), which by the end of 1995 had made 141 minority equity investments in small business ventures. AAC's small business unit (SBU) claims it has created over 300 business opportunities for SMEs, with total sales of over R205 million and has generated 3,600 jobs over a five-year period.

Anglo-American is not the only corporation in the RSA that has launched a small business support initiative. Other corporations, public and private, that have developed small business programmes in the RSA include Sasol, the public energy company; Eskom, the electrical corporation; Hoechst, the chemical multinational (see Annex 2); Transnet, the transport conglomerate; DuPont; Texaco; Caltex and SA Breweries among the foremost.

Sasol started a small business unit (SBU) in 1991 and claimed by 1995 to have created 39 new small businesses, mostly by "spin-off" of functions previously performed in-house. The SBU's activities, although initiated for social objectives, is also driven by "contracting out" commercial activities resulting in savings of 15-20 per cent in the cost of the affected activities. Among the services previously performed in-house and now carried out by outside owner-operated businesses are: office cleaning and maintenance, ash disposal, gardening, painting, printing, catering, the recovery of process materials, internal transport, security, parking, pallet supply and repair, drum reconditioning, etc. Some, but not all, of the entrepreneurs had previously run or worked in the same activities as company employees but had no relevant business experience. The help of the large corporation was in all cases of great importance to the success of the venture. The SBU assisted these businesses in conforming with legal requirements, helped them to obtain finance (from banks), provided and arranged business training, and drew up contracts between Sasol and the entrepreneurs stipulating prices, delivery times, quality and payment terms.

Sasol also engaged in a joint development with SBDC in developing a small industrial estate at Sasolburg (the town where Sasol operates), housing 25 small businesses, most of which supply a service to Sasol.

Other interesting small business support programmes carried out by corporations in the RSA include the following:

- a programme by Caltex (which supplies 18 per cent of the oil products used in the RSA) to help black entrepreneurs set up and own petrol service stations. Of 1,100 Caltex service stations, 264 (26 per cent) are now (1996) owned and operated by "non-whites";
- South African Breweries (SAB) in 1987 piloted an owner-driver scheme in Cape Town to create self-employment for eight truck drivers. Since then some 100 SAB truck drivers — 20 per cent of the total — employing 450 crewmen have been set up as independent businessmen, taking ownership of the trucks they used as employees of the company. SAB also set up 14 different independent distributors of its products;
- ESKOM has, since October 1992, actively supported the development of small black-owned businesses to help in job creation. Examples of the type of businesses established include: vending agencies for the sale of metre tokens, small appliance repairers, poles setting for electrification, contractors for electrification of schools, welding, bakeries, cabinet making, food preparation, transport. ESKOM identifies business opportunities, then networks with a funding agency and arranges training through an appropriate institution. ESKOM only helps registered businesses. By 1995, 75 small black-owned businesses were regular suppliers to ESKOM. These cover: computer equipment and accessories, the manufacture of dust coats, the supply of best meat, security services, horticultural and landscaping services, cleaning, etc. Some joint ventures of white suppliers and black entrepreneurs have also been created.

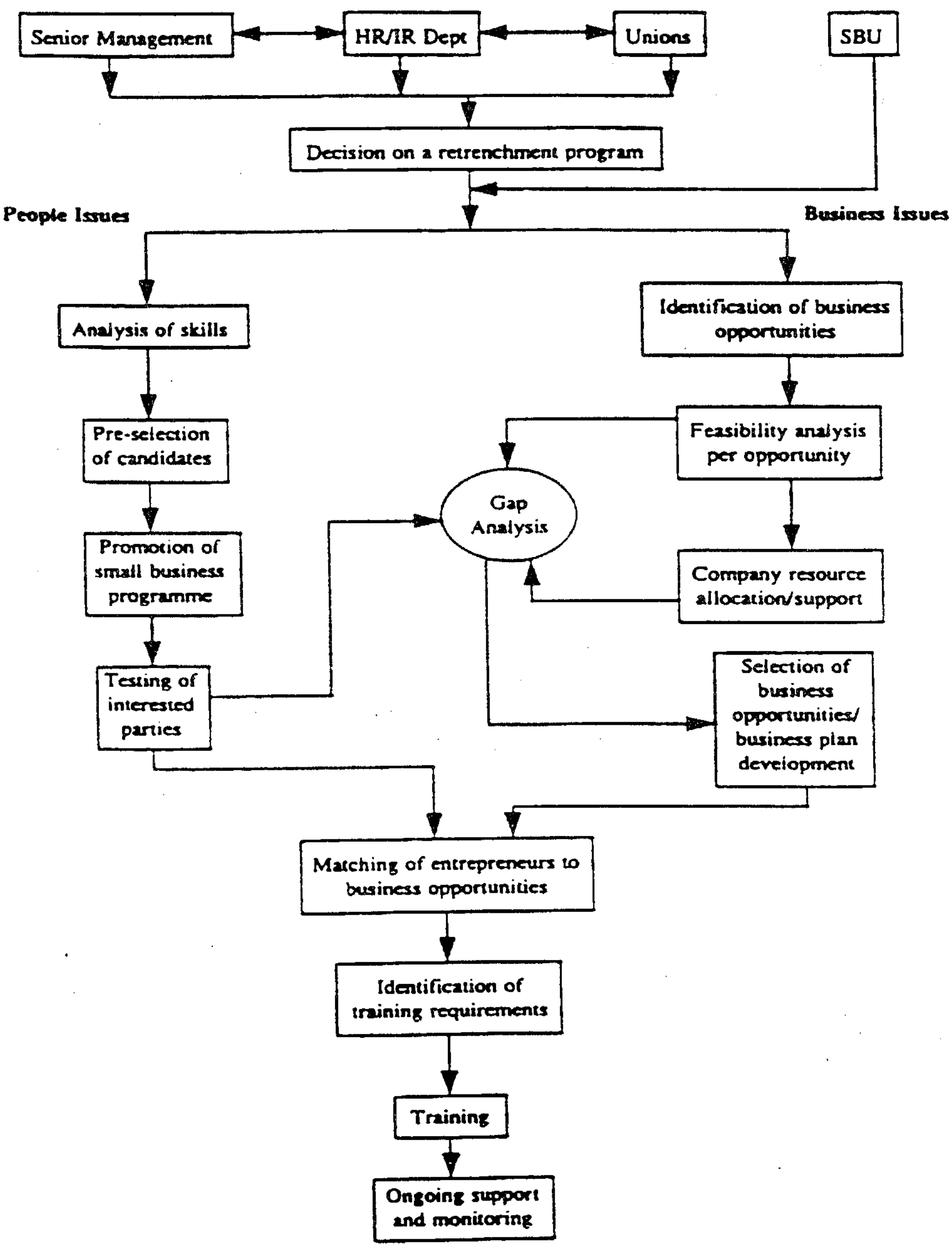
Small business development among retrenched workers

These are the lines of special programmes used by SNU in the RSA for setting up small businesses using "retrenched" employees. As can be seen from the chart presented here, the process is one of matching the candidates among the employees "retrenched" in restructuring and "down-sizing" of large corporations who have the requisite skills, motivation, business and technical abilities to make a success of an identified small business opportunity.

The process, as the chart shows, involves "people issues" — the identification, selection and training of suitable former employees to enable them to set up and run effectively the small business and "business issues" — identifying and establishing appropriate businesses and allocating the resources to these businesses.

The two cases given in Annexes 2 and 3 are examples of two major corporations who carried out such programmes to help retrenched/redundant employees to set up in business.

The functions of a SBU in setting up S/B opportunities using retrenched employees



Source: C. Mantle and C. Ryan, (1995): "Interacting big and small: South African corporations involved in small business development", BMI Rivonia, South Africa.

The banks

The major South African banks — Standard, Nedcor and First National — each have small business units that offer finance and advice to small businesses (SB).

Standards SB Development and Advisory Department (SBDAD), set up in 1982 has helped 5,000 new businesses employing around 50,000 workers. Of the businesses assisted, 35 per cent are black-owned. Only a small number of the businesses helped by SBDAD have failed and bad debts of SB borrowers are less than 2.5 per cent. Over 90 per cent of loan applications are for new businesses.

Similarly Nedcor Enterprise was launched in 1991 and started a consultancy division in December 1993. Nedcor Enterprise has helped small businesses to become involved in subcontracting and has also promoted and financed franchising operations.

First National Bank (FNB) has had a small business unit since 1979 and tries to link many small enterprises among its lenders to large corporations. FNB had reported a phenomenal increase in finance applications since mid-1993, many introduced through the large corporation small business initiatives.

6. Developing countries

As might be expected, there is less collaboration between large and small businesses in developing countries. The small enterprise sector is much weaker and less able to supply products and services at the standard required by large enterprises. Although unemployment (and under-employment) is rife, there are fewer cases of major retrenchment of labour due to structural changes in larger corporations, although there have been some cases of the closing down of mining operations, and of course government shedding of employees after structural adjustment programmes.

After a period in which the multinationals (MNCs) operating in Third World countries were seen as exploiters of the resources and contributing little to the development of the countries and to the welfare of the people, by the 1980s, the attitude had changed as the MNCs themselves became more sensitive to the need to contribute to local business development. Accordingly, several MNCs have begun to help with SME development.

India and South-East Asia

India provides some interesting examples of activities of large corporations in cooperating with SMEs. The Indian affiliate of Philips, the large electronics MNC, claimed, by the end of 1989, to have helped small-scale units to develop as independent suppliers to the company. The corporation helped these SMEs with arranging finance and improving the products technically, enabling them to introduce new production methods. Siemens, the German MNC, also helped develop 1,000 local suppliers, raising their quality standards, expanding the range of their products and providing them with improved tooling.

Not only have foreign-owned corporations assisted small industries in India, some local large companies have also developed assistance programmes of this type. Glyndia (formerly Glaxo Laboratories) has helped small producers to produce new products based on original research undertaken by the company. Glyndia has helped these small and medium producers to upgrade product quality, often with help in acquiring more advanced equipment and facilities.

In recent years India has acquired a significant high-tech industry, especially in the field of computer software. Many of these businesses are built up by former employees of the large foreign-owned computer firms with the collaboration and assistance of their former employers. Ingersol-Rand, the United States MNC's Indian operation helps employees to set up independent units to manufacture components and sub-assemblies, in many cases selling to them used machine tools át advantageous terms. This is one case where the larger company used this approach to reduce its own workforce.

One firm that has been known throughout the developing world as having a corporate philosophy of social commitment to the countries where it operates is the large footwear manufacturer, Bata, which has built manufacturing plants throughout the developing world. Bata has not only produced footwear suitable for people of developing countries at relatively modest prices, but has also built up a network of independent shoe retail businesses in countries such as India, Malaysia and Kenya. The firm has also generated a range of "spin-off" small firms manufacturing shoe and footwear components and has helped train unemployed youths to become entrepreneurs.

The large Indian-owned corporation, Birla, was the prime mover in setting up the Small Industries Research and Development Organization and the Birla Institute of Technology where engineering graduates are encouraged to set up SMEs. Such entrepreneurs receive technical and managerial help from both the above Birla-assisted organizations.

Unilever, the Anglo-Dutch food and household goods multinational, was one of the first corporations to try to offer help to local small businesses in Africa. In Kenya they helped organize KMAP, the Kenyan Management Assistance Programme, a group of 90 larger companies including BAT, Kenya, Ciba-Geigy, Nestlé and others, to advise and guide small enterprises facing problems.

There are similar organizations in other developing countries. The Philippino Business for Social Progress (PBSP) is an institution of large businesses set up in the early 1980s wherein each member company commits itself to set aside 1 per cent of annual net profits for social development, of which 60 per cent is given to PBSP. During the five-year period, 1986-91, PBSP supported 140 micro-enterprise projects with small amounts of equity, loans, training and advice.

Latin America

There are many examples of large enterprise support of SMEs and micro-enterprises in Latin America (LA) and foundations have been set up in various cities and countries offering financial and technical aid to micro-enterprises. The informal micro-enterprise sector provides incomes and occupations for over 50 per cent of the workforce in many LA countries, e.g. Peru, Bolivia, Colombia, Ecuador, Mexico. Foundations such as Carvajal in Cali, Colombia is one of 24 different foundations operating in the cities of Colombia, supported in most cases by larger businesses providing loans, training and technical assistance to micro-enterprises. Although employment creation in such micro-enterprise programmes is less than in support for formal SMEs, the micro-businesses helped to resolve subsistence and employment problems for large numbers for whom the formal economic sector could not offer alternative employment. Similar foundations supporting micro-businesses are active with help from external donors or NGO assistance in Peru, Ecuador, Bolivia, Dominican Republic, Brazil, Guatemala and Mexico (as well as Colombia).

Some multinationals have also assisted local SMEs in Mexico, Brazil, Argentina and the Caribbean countries, such as the Singer Sewing Machine Company which has helped the development of cottage industries through the sale of their machines in rural areas. The company helped by adapting Singer machines to local sewing and knitting skills. The machines were offered, combined with training, to village women at favourable credit terms.

Africa

As stated earlier, there are far fewer examples in Africa of collaboration between large corporations and SMEs, although there are some cases (as in Kenya mentioned above). The United Kingdom multinational Lonrho's large textile manufacturer David Whitehead in Malawi provided its engineers to small local firms in Malawi to help them install and operate equipment which had been beyond their technical competence. With the technical assistance provided, two small firms were able to start producing shoe laces and bandages.

In Zimbabwe, a large paper factory took over a small fruit and drink producer, employing 25 persons, which was making big losses and was about to go out of production. With considerable technical assistance from Hunyani, the large paper producer who also invested new capital and helped with marketing the products, Sunsplash, the small drinks company, was turned around and became profitable.

The South African experience (see Chapter 5) shows that the most effective way for large corporations to help generate new small businesses and answer their profitability is through the creation of a special unit or division. There are, of course, difficulties in finding suitable staff who can adapt the experience of the successful large corporations to give appropriate advice to small businesses or micro-enterprises. In some cases the process may be helped by support from intermediary organizations, usually foundations or NGOs of which there are examples in Latin America (see above) and the cases of KMAP in Kenya and PBSP in the Philippines.

Several African countries have gone through major structural adjustment programmes which have created large numbers of redundancies among government employees. Ghana is a major example and programmes were developed to encourage these retrenched government workers to become self-employed and to start their own businesses. Although the programme provided credits as well as business training and advice, the outcome was relatively modest, mainly resulting in a small number going into self-employment or starting some small service micro-businesses. In this experience women proved more entrepreneurial in starting micro informal units.

Subcontracting links

In most developing countries, subcontracting linkages between large and small enterprises are very weak. In the least industrialized African and Asian countries, this is mainly due to the lack of the type of large manufacturing firms that could help generate suppliers of components and services.[1]

Even in countries that are more developed industrially, where large vehicle, appliance and machinery manufacturers exist, that in developed countries would expect to subcontract a considerable part of their production, these either depend on imported inputs or are virtually integrated (i.e. produce all items in-house). In fact, in developing countries it is more usual to find subcontracting in traditional industries such as the production of garments, shoes and furniture where medium and larger firms give out work to cottage industries and micro-enterprises to take advantage of much lower labour costs.

Larger firms tend to have little confidence in the reliability of SME suppliers as regards quality, delivery and in many cases even price (compared with imported items). There are even many instances of MNCs inducing their regular international suppliers to set up production in the developing countries concerned (Malaysia and Thailand have several examples of Japanese component producers setting up in these countries). Specialization among local SMEs in these countries is still rare.

As more developing countries liberalize their trade and import regimes, there are signs that the competition of overseas suppliers is driving the traditional SMEs out of business. Governments need to be aware of this development and should adopt measures to promote supplier relationships between SMEs and large firms through helping to develop greater competitiveness.

Policy-makers must try to identify firms that are considered to be capable of upgrading their performance to compete with imported items, even if for some period these SMEs may need special help from public agencies and large firms (preferably the potential contracting or parent firm) who should be persuaded to offer assistance.[2]

In some developing countries it has been found that where SMEs that are potentially suppliers with competitive advantages form part of sectoral/regional clusters they can benefit from a range of positive effects of working with other similar small firms. There is strong evidence that the encouragement of such "clusters" can prove effective, making it easier to direct specific measures to assist them. In the case of the manufacturer of the Malaysian car Proton special efforts were made to match local firms with reputable foreign manufacturers to upgrade their technical capability so that they can manufacture high-tech automotive components. Altenburg sets out possible policies for the "promotion of ancillary industries". He recommends providing information on subsidies for hiring specialized consultants (which should be made available), access to data on potential subcontracting through subcontracting exchanges that match supply and demand and on sources for advice and technical assistance.

[1] Since subcontractors or suppliers are called in India and some other Asian countries ancillary industries. See Altenburg (1997).

[2] ibid.

Apart from these, exchange fairs or exhibitions can be arranged, as in the case of Mexico, where large manufacturing firms exhibited "knocked down" parts of their final products — from electronics to garments — to SMEs who are invited to bid to supply components and sub-assemblies.

It is important not to impede the emergence of local suppliers and subcontractors by inappropriate fiscal incentives such as are often given to firms in "export processing or free trade zones" who are allowed to import tax-free imports while the same items from local firms are subject to tax. Taxes on total sales value of products encourage foreign firms to concentrate on as many stages of value added as possible "in-house". A "value added" tax will at best create an equal treatment between local and foreign suppliers.

Local content requirements have been used by governments to encourage foreign investors to use local suppliers, but quality considerations and pressure to liberalize trade have forced government to reduce such policies.

Some countries have offered incentives, benefits, subsidies, tax deductions or preferential treatment in public procurement to large firms willing to invest in the upgrading of supplier firms that source supplies from local SMEs, but these incentives do not appear to have produced significant results. The Indonesian Government has tried a Foster Business Partner Linkage where the large foster firm helps with the adopted SME in management and technology, acts as a guarantor for bank loans and help with marketing the SME products but this scheme too has had only limited success. An interesting case is that of Mexico's "Supplier Development Programme" of NAFIN, Nacional Financieria. If potential suppliers present viable projects NAFIN will cover 50 per cent of the credits. A "factor" scheme also enables suppliers to discount bills issued by contractors. NAFIN in turn guarantees up to 50 per cent of losses suffered by contracting firms due to defective performance of their suppliers and makes available low-interest funds to large companies to finance credit, training and technical assistance for their suppliers.

Finally, some large contracting firms with a high number of subcontractors and suppliers may actually help set up special industrial estates for the "ancillary industries". This has been done in India, Singapore and Mexico, mostly in the vicinity of large car or machine tool manufacturers.

7. Conclusions and recommendations

Unemployment is the scourge of modern economies. Both in developed and developing countries, including most middle-income countries and economies in transition, the formal economy as driven by market forces alone has proved unable to provide jobs for the rising population. In addition, the rapid pace of advances in technology, whereby automation is replacing manpower, and global competitive forces are driving firms to restructure and slim down their workforce to the minimum, thus increases the number of unemployed.

Structural reform has shrunk the role and size of government, compounding the problem. So have waves of privatization in various countries which invariably lead to large numbers of redundancies in the workforce of firms as the ownership is moved from the public to the private sector.

In developing countries there is a further problem. Most new jobs in the more advanced countries are created in the service sector. Many of the services are inevitably poorly developed in the Third World, especially in such fields as the financial sector, retail distribution, leisure, entertainment, personal transportation and so on, all of which employ significantly less people in developing countries.

The solutions are not easy and must be long term. In market economies, governments are *not* the main creators of work, so that only a public-private sector partnership and collaboration can feasibly attempt to tackle the employment problem. This partnership is apparent in many of the schemes described in earlier chapters and in table 4, which gives the main actors involved in implementing each type of programme listed.

Table 4 summarizes the main types of programme discussed in earlier chapters and indicates examples of organizations and countries where each strategy has been attempted, with what success. What follows is a summary of the lessons learned in relation to each strategy.

Financial assistance to small businesses

Business development in the form of both "start-ups" and business expansion are essential. As large firms, either through privatization or restructuring, shed part of the workforce, the parent enterprises undergoing the employee retrenchment must be induced to initiate and help to implement programmes to provide alternative livelihoods for those made unemployed.

The South African experience demonstrates that the creation of a "small business unit" (SBU) or division — with top management active support — can be a most important step forward. Subcontracting, or "outsourcing" the purchase of services and other inputs from smaller businesses should be the first fields of activity of the SBU, but it is important that the unit does not in the longer term confine itself to these areas. As in the case of some of the larger corporations in South Africa, these firms should be made to understand by government and local authorities that major businesses and employers in an area are expected to contribute to the welfare of the community from which they obtain their workforce and much of their commercial support. Helping to set up appropriate business support centres, possibly a local equity fund and collaborating in a business incubator or industrial estate are just a few of the ways in which the major corporations can assist in local business development, and help create new employment opportunities in start-ups and expanding small enterprises.

In some situations (e.g. British Coal and British Steel), the parent company's eventual complete withdrawal from an area has meant that large-small supplier and subcontracting linkages were impracticable; however, the continuing involvement of the investment company (British Coal Enterprise and British Steel Industry) in attracting small businesses with growth potential into the affected region has produced many employment opportunities.

In many countries the parent company does not have the resources available to set up a local investment fund, and it is in these situations (for example, in CEE/FSU and developing countries) that governments or international donors may have to provide the investment. What is common to all such funds is that it takes time to achieve results. The hundreds of investments, and thousands of jobs created or saved by companies like Elf-Aquitaine's SOFREA or British Coal (see table 4), have taken place over ten or 20 years. New funds, such as the Equity Investment Fund in Poland, may take two years to make only two investments, since experience is needed for making successful local investments. Similarly it takes time for credit guarantee companies to build up a basis of trust with the local banks. In principle, however, established credit guarantee funds should be able in due course to leverage five to ten times their volume in loans for small businesses from the participating banks. Faster results are sometimes achieved with direct lines of credit (for example, EBRD's Russia Small Business Fund, which has managed to disburse 10,000 loans in three years), but without the leverage possible with credit guarantee schemes.

Local development agencies

The success of such local investment funds depends partly on the availability of technical support and business advice and training for the small firms involved. Evidence shows that the establishment of a local enterprise agency or regional development agency can be of considerable help. The agency or development corporation should be set up with significant equity and management cooperation from the local or regional authority with some central government, social or regional development funds available. Private local capital should be sought from large corporations and preferably banks operating actively in the area, especially from the companies engaged in workforce reductions.

The development agency office should maintain active contact and consultation with local business associations, chambers of commerce (who may participate directly in the development institution). Help in organizing training programmes and business advisory services should be mobilized from business schools, higher educational institutions and consultancy groups. In particular, local corporations should be asked to second professional staff (full or part-time) to the development agency to provide advice and help in preparing business plans (for "start-ups" and expansions), in negotiating with banks, official assistance schemes and in obtaining support from other local companies in locating premises and other inputs required for launching the project. As well as advising small businesses with growth potential, the local agency or corporation created should provide a "one stop" advisory service for the unemployed, especially for those contemplating self-employment or setting up a small business.

Spin-offs

Evidence suggests, in the cases reviewed in this paper, that most success in new small business development arises when, after restructuring in a large corporation, either following privatization, take-overs, mergers or a major reorganization to reduce losses and "turn around" the enterprise, "spin-offs" of separate cost centres take place. As shown in some of the examples given, services such as gardening, catering, building maintenance, printing, security or transport services can be "hived off" successfully when those who have been responsible for the activity in the parent firm are encouraged and helped to set up independent businesses to supply the same service from outside the company. It has been shown that if the parent firm provides some equity (normally less than a controlling interest and often from an independent venture capital fund), and — equally importantly — provides some transitional retainer service contract, such ventures have a higher success rate, especially as those who manage and are engaged in the business have previous experience in providing the service.

So far, "spin-offs" of the type described above and others more directly related to the manufacturing process (e.g. product design, computer services, laboratory analysis, accounting and quality control, as well as production of components, packaging or special finishing processes) have not taken off to a great extent in the transition economies, largely because of the long tradition of integrated enterprises with virtually all services performed in-house. This situation, together with inadequate business background and experience of those who could potentially take over "spin-off" operations, and a lack of confidence of those managing the large enterprises in the quality of an outside service, explain further the slow development of "spin-offs" in these countries.

In these situations management consultants can help, first of all by helping the large enterprise manager come to accept the fact that the "down-scaling" of the parent enterprise is unavoidable in a market economy, and then by helping him identify which parts of the enterprise might still form profitable cost centres as independent businesses. Management consultancy of this kind has been provided by expatriates until now (e.g. in Romania), but gradually such expertise is being transferred to local business support agencies.

A lack of available private finance also impedes the growth of "spin-offs" of discreet operations into independent smaller enterprises during privatization. Foreign investors might be encouraged to become involved, but this would probably be only for larger "spin-offs". Equity funds of the types referred to above could be of help.

Management buy-outs

In Western Europe and North America, management buy-outs (MBOs) have taken over larger plants that have faced closure with the possibility of large numbers of job losses. In these cases, the MBOs, consisting of all employees contributing (as in the case of ESOPs) or groups of managers and professional employees, aided by other investors and leveraged by large bank loans, have taken over ownership and have managed to continue operations on a much reduced scale, generally with less than 50 per cent of the former employees.[1] Earlier leveraged MBOs have only been partially successful: less than 50 per cent have survived under the management ownership beyond a few years according to one estimate,[2] but this is now the most common vehicle for investment in reviving loss-making corporations by venture capital funds in Western Europe. More recently MBOs have had a better success rate. Greater sustainability of MBOs may be achieved if the project is adequately capitalized with equity funding and not leveraged too highly with loans.

The purchasing of shares by employees through ESOPs is an increasingly popular strategy in the United States for management buy-outs to take place to avoid hostile take-over bids and plant closures. Evidence shows that ESOP-owned businesses are no more reluctant to consider job losses than other businesses. However, sometimes they also perform better than other businesses, and this can result in new jobs arising subsequently.[3] ESOPs that combine employee ownership with a participatory form of management also are shown to perform better. ESOPs are also being used in the privatization process in countries in transition (e.g. Hungary) and here they have the important effect of increasing economic democracy, and involving employees in the ownership of their company.

[1] Bradley and Gelb (1986). However, other surveys estimate initial job losses at only 6 per cent (Wright, et al., 1992). Both sources agree that after the initial period, most successful MBOs are able to increase their employment.

[2] Bradley and Gelb (1986).

[3] Hansen (1993).

Self-employment schemes

There is a greater potential for a diverse local economy and for more secure jobs through investing in business expansions (with a success rate of over 80 per cent, in the case of British Coal Enterprise) than through supporting self-employment (with a success rate of 64 per cent).[1] Also, the numbers of jobs created by growth-oriented businesses (e.g. an average of 24 jobs created per business funded by SOFREA — see table 4) compares favourably with the one or two jobs that might be created in a typical micro-enterprise.

With many industries, however, redundancies may be spread throughout the country, making a regional investment policy difficult. Self-employment may be a preferable alternative to unemployment for many redundant workers from these or other industries, or it may be a temporary solution until a better job opportunity arises, and these people should be given suitable assistance. Investment fund managers from the parent company are often not interested in financing self-employment ventures, because of their lack of profitability, and it is here that governments should play a greater role.

Schemes that provide financial support for the early days of self-employment, or a lump sum to help with the purchase of equipment, usually have a positive effect on business success rates, provided that they are combined with business advice services (64 per cent success rates as against 40 for all business start-ups).[2] Business training and follow-up should be provided by local private sector development agencies, with funding provided by government. Such agencies play the essential role of screening out applicants whose business propositions look set for failure, thereby reducing unnecessary wastage of public funds, and also dissuading the applicants from embarking on a course that might lead to overwhelming debts.

The role of government

In most countries undergoing structural adjustment programmes, which usually involve government workforce reductions, the privatization of poorly run state enterprises, liberalization of both internal and external trade and various means of liberalization, it is now generally recognized that there is a need for urgent measures to counter the rising unemployment caused by all the changes. This should involve the creation of a social fund by government, generally substantially supported by donor contributions.

The fund should cover the following areas:

- training and retraining programmes to orientate those who have been skilled or semi-skilled workers in fields for which there are no further prospects of employment (e.g. coalmining, steelmaking, glass manufacture, etc.) towards business creation and management according to the prospects and aptitude of the jobseekers. Suitable training institutions are often in the private sector; and where possible this training should be funded by the parent company. However, a degree of subsidy by government is usually necessary;
- regional-based programmes channelling business funding and rate and rent incentives into areas of high unemployment can be successful in regenerating these areas;[3]
- financing self-employment programmes for the unemployed.

The compelling evidence shows that public-private partnerships and collaboration between the sectors produce the best results. Nevertheless, there is a major role for government in business development and job creation. It is often repeated by economists who believe strongly in the market, that governments do not really create permanent sustainable productive jobs; only

[1] Coopers and Lybrand (1995).

[2] ibid.

[3] Made (1996).

the private sector can do that in a market economy. While this may not be strictly true in all situations, it is a fact that the private sector is the main generator of jobs in most conditions.

However, the government can stimulate private business development and employment growth by fostering an "enabling economic environment". This means minimum regulations; fair, broad-based taxation as low as feasible and simple for compliance; liberalized trade both domestic and external, and helping to create a financial sector with easier access to funds for all businesses. The government should also make available funds (along the lines of the social fund mentioned above), including lines of credits for small business loans to mitigate the damage to businesses and of employment losses created by policy reform and restructuring. The government should act as a facilitator — a provider of resources — for support and advisory centres, but not as a direct provider of services. The government is also responsible for creating the physical infrastructure — roads, power, water, transport links, telecommunications, industrial land, estates and incubators — and basic skills training and satisfactory education at all levels. Without these, the private sector cannot flourish. It is important to recognize that the provision of some of the above facilities may be the responsibility of local or regional authorities as well as central government. The decentralization of support services and the encouragement of regional and local initiatives is desirable and usually more cost-effective.

References

Altenburg, T. (1997). "Promoting ancillary industries in developing countries", in *Small Enterprise Development,* Vol. 8, No. 2.

Bradley, K.; Gelb, A. (1986). "Share ownership for employees", Public Policy Centre, London.

British Coal Enterprise (1996). *The enterprise years: The story of British Coal's job-creation company.*

British Steel Industry (1996). *Twenty-one years of going for growth,* British Steel Industry Ltd., Sheffield.

Brockaw, L. (1993). "The truth about start-ups" in *Inc.,* Vol. 15, No. 3.

Business Link (undated). *Getting the best from your business.*

Charap, J. (1992). "Entrepreneurship and SMEs in the EBRD countries of operation" , EBRD, London.

Coopers and Lybrand (1995). "Do local enterprise agencies add value to clients?", report undertaken by Coopers and Lybrand for the National Federation of Enterprise Agencies.

Drury, D.; Walsh, S.; Strong, M. (1993). "Evaluation of the EDWAA Job-Creation Demonstration", prepared by Berkeley Planning Associates, for the United States Department of Labor, Washington, DC.

Forbairt (1995). *Annual review 1995.*

Futo, P. (1997). "The role of credit guarantees in financing Hungarian small businesses", in *Small Enterprise Development,* Vol. 8, No. 2.

Gibb, A.; Lyapunov, S. (1995). "Creating small businesses out of large in Central and Eastern Europe", in *Small Enterprise Development,* Vol. 6, No. 3.

Gibson, T. (1996). "Equity and venture capital financing in countries in transition", in Levitsky (1996), op. cit.

Graham and Trotman (1989). "Partnerships between small and large firms", Commission of the European Communities, London.

Hansen, G.B. (1993). "ESOPs in the USA", presentation to the ILO seminar "The economies in transition and the employment problem: The role of cooperatives and associations", Kiev, Ukraine.

— (1994). "Joint labour-management training for successful bottom-up privatization in central and eastern Europe: A proposal".

Hubner, D. (1996). "Institutional support for small business in Poland", in Levitsky, J. (ed.) *Small business in transition economies,* Intermediate Technology Publications, London.

Lichtenberger, B. (1992). "Active labour market policy: Enterprise management contribution", ILO, Geneva.

Made (1996). *Annual review 1995/96,* The Valleys Enterprise Agency, Made.

Mantle, C.; Ryan, C. (1995). "Interacting big and small: South African corporations involved in small business development," BMI, Revonia, South Africa.

Morgan, K. (1994). "Reversing attrition: The auto cluster in Baden-Württemberg", Arbeitsbericht, Akademie für Technikfolgenabschätzung in Baden-Württemberg, No. 37.

Nelson, E.; Taylor, J. (1995). "New ventures and entrepreneurship in an eastern European context: A training and development programme for managers in state-owned firms", in *Journal of European Industrial Training,* Vol. 19, No. 9, MCB University Press Ltd.

Nelson, E.; Cornel, M.; Pearce, I. (1997). "The singed phoenix — Managing company disaggregation and spin-offs in a transition economy", book awaiting publication produced by Durham University Business School.

OECD (1995). "International seminar on local system of small firms and job creation — Background paper", OECD, June 1995, Paris.

Paukert, L. (1995). "Privatization and employment: Labour transfer policies and practices in the Czech Republic", Labour Market Papers, ILO, Geneva.

Rosenfield, S.A. (1994). "Industrial strength strategies: Regional clusters and public policy", produced by Regional Technology Strategies Inc.

3I Group (1996). *3I Group plc company facts.*

Vyakarnam, S.; Jacobs, R. (1993). "Teamstart — Overcoming the blockages to small business growth", winner of the Stan Mendham Award for Best Policy Paper at the 16th national Small Firms Research and Policy Conference, Nottingham.

Webster, L. (1992). *Private sector manufacturing in Hungary: A survey of firms*, Industry Series Paper No. 67, World Bank, Washington, DC.

Welch, C. (1997). "Information on Grosvenor Career Services", document prepared for Grosvenor Career Services.

Wilson, S.; Adams, A.V. (1994). *Self-employment for the unemployed — Experience in OECD and transitional economies*, World Bank Discussion Papers No. 263, Washington, DC.

Wright, D. (1989). "Collaboration between multinational and small enterprises", ODA, London.

Wright, M.; Thompson, S.; Robbie, K. (1992). "Venture capital and management-led, leveraged buy-outs: A European perspective", in *Journal of Business Venturing,* Vol. 7, No. 1.

Annex 1

Spin-offs in Romania

Case 1. Ecosib SA — Creating a separate profit centre

A new company, involved in the collection and disposal of domestic and industrial waste, has already been spun off from a local authority public service organization. The managing director is finding that the company is under pressure from competitors, and that part of the problem is the constraints his company is under in dealing with their former owner, the local authority, and another source of inefficiency is the large waste-disposal side of the operation. He decides to set up the waste processing and disposal part of the operations as a separate profit centre and a wholly owned subsidiary, Ecosib SA.

Case 2. Scug SA — Spinning off ventures without needing capital

Before its markets shrunk, Scug SA was one of the largest heavy construction equipment companies in Europe, owning extremely valuable equipment that was now lying around largely unused. The general manager felt that the best way to gain contracts was to make the managers of the operating divisions responsible for expanding their own markets by turning the divisions into separate private companies. None of them could raise the capital to purchase the equipment, so the solution achieved was to lease the equipment to the new companies who would pay hire charges for their use. The actual terms of the deal that emerged, however, were not always welcomed by the prospective managers.

Nevertheless, one of the new private management companies which was spun off, Romprest SA, has proved very successful. The state owners of the equipment have decided not to extend the lease on the equipment, however, but to insist that Romprest SA buy the equipment. In view of the success of the business, a high value has been placed on the machinery, and Romprest is unable to purchase it outright. The managing director has been faced with a number of options, such as paying for the equipment by instalments, and must make a decision about how to proceed.

Case 3. Cab SA — Turning an under-used asset into a profitable business

The managing director of Brasovia Auto Services witnessed the volume of trade in auto spare parts and warranties diminish to one-tenth its earlier size, and with customers having trouble paying for the work done. As a result, some of Brasovia's capacity, including a warehouse and some land, were no longer used. The process of gaining permission to change the use of the warehouse was time-consuming, involving dealings with the state bureaucracies, but at the end of it the warehouse was converted into a commercial centre, with space for 86 units. Leasing this workspace is proving much more profitable than the manufacturing side of the operation.

Case 4. Oxi-Ers SA — A joint venture to develop markets

Oxi-Ers SA was originated from an oxygen plant which formed part of a large steel casting and manufacturing company, making heavy industrial machinery. As a result of restructuring, the oxygen unit remained with the services division including road and railway maintenance and energy supply. A western marketing and distribution company is interested in the oxygen plant as a separate unit, and proposes a joint venture, by which Oxi-Ers would become a producer under its control, supplying oxygen to the distribution company. This option raises questions of whether the parent company would still be supplied by the oxygen plant, and how Oxi-Ers would be allowed to develop. An alternative would be for Oxi-Ers to develop its own distribution division, but its managers think that this option is beyond their expertise.

(Annex 1 is taken from: Nelson, E.; Cornel, M.; Pearce, I. (1997). "The singed phoenix — Managing company disaggregation and spin-offs in a transition economy", book awaiting publication produced by Durham University Business School.)

Annex 2

AECI

Between 1989 and 1992, AECI's Modderfontein plant retrenched 2500 workers, reducing its manpower complement to 5,000. A three-pronged programme was implemented to soften the blow to workers who lost their jobs:

- to redeploy workers within the group where possible;
- to retrain workers for other work;
- to identify and assist in the creation of small business opportunities.

Many workers received generous "redundancy" benefits and returned to the traditional areas, some to retire, others to open up businesses such as butchers, discos and convenience stores, without any assistance from AECI.

AECI set up a small business unit (SBU) and invited approaches from employees about to lose their job who were interested in setting up small businesses. The invitation elicited a muted response, requiring a more proactive approach by the SBU in identifying business opportunities and selecting entrepreneurs. This programme resulted in the creation of seven small businesses employing former AECI staff. A further 20 external suppliers were also helped to set up in business.

Company policy stipulated that the AECI's buying staff should support small businesses where "such purchases could be made or services secured to meet requirements at lower overall cost". Limited financial assistance can be extended from the company's "quality of life" budget where no external sources can be found. AECI does not act as banker and expects the entrepreneur to share risk. The following assistance was provided in terms of the company policy which was applicable during the period of retrenchments:

- surplus or redundant equipment may be used by entrepreneurs for no cost, or an agreed loan rate;
- the provision of premises, if and when available, at market-related rates;
- the SBU provides mentoring services to small businesses;
- training (e.g. how to start your own business) may be provided through AECI at minimal cost to the entrepreneur.

Annex 3

Hoechst

Since the mid-1980s, the chemical corporation Hoechst's business development unit has set up 30 small businesses employing more than 300 workers in relatively high-tech markets as part of its social investment programme. Unlike Anglo American, Hoechst sources little of its supply needs from these businesses. There are no cost savings or productivity benefits which accrue to the company as a result of its small business efforts, so these activities correctly fall under the heading "social investment". In the words of a business development services manager, this is Hoechst's contribution to the creation of a stable and prosperous society.

Blacks had relatively little experience in manufacture and there were doubts as to the quality, consistency and reliability of supply from these entrepreneurs. It was found that black entry to the formal market was barred because they could not meet the strict requirements of this market (e.g. parastatals generally require suppliers to conform with SA Breweries' standards, which is a costly and complicated procedure for small enterprises). Furthermore, large retailers have complex requirements for suppliers. They must buy shelf space, offer substantial discounts and incentives, and payment periods are generally protracted.

Hoechst decided to use its corporate muscle to open doors for small black-owned businesses to the formal sector. It offers three types of assistance:

- negotiating contracts with corporations to source products from the small businesses created by its small business unit;
- approaching large retail chains on behalf of its entrepreneurs to get the stores to stock products;
- bulk supply to large customers such as mines and parastatals. Fingers Chemicals was established (together with Anglo American's small business initiative) to supply industrial cleaning detergents to the nearby De Beers mine.

(Annexes 2 and 3 are taken from Mantle, C.; Ryan, C. (1995). "Interacting big and small — Why South African corporations should get involved in small business development", BMI Industrial Consultancy, Rivonia, South Africa.)

Annex 4

The automobile cluster in Baden-Württemberg

In 1991 the car industry in Baden-Württemberg employed 250,000, mostly in the area around Stuttgart, which represents around a quarter of all auto workers in Germany. The cluster depended to a large extent on a few major employers, notably Mercedes-Benz, Porsche, Audi and Bosch. After years of consistent growth and prosperity, the industry has been in a deep recession since 1991, resulting in the loss of over 33,000 jobs. These lay-offs were part of a broad attempt by the German car industry to reorganize itself in the face of competition from Japan and elsewhere.

The restructuring of many of these large corporations has had a severe impact on smaller suppliers and component manufacturers in the area. One reason for this is the move to single and modular sourcing, which means that only a few suppliers are now "first tier", and these will, by necessity, be larger enterprises able to deliver a wide range of components and services. This has endangered the celebrated relationship between the large multinationals and the small local suppliers. Small firms in the area can now only meet the supply needs of the car manufacturers by grouping together to reach the scale and variety of product required. However, in many cases, the SMEs jealously guard their independence and are unwilling to enter cooperative arrangements. To overcome this, the regional government has acted to implement a series of joint initiatives agreed between the Land government and representatives of industry and labour. The first of these joint initiatives, started in 1992, underlines the need for:

- better information flows to improve awareness among smaller suppliers of structural reforms and their consequences;
- a fund (initially DM4.5 million) to address the specific problems of small supply firms and help promote new production and management techniques;
- a series of well-funded, technology-oriented research projects;
- research into "lean production" management techniques to help disseminate best practice and ensure that all links in the supply chain are working under the same precepts;
- strategic alliances and cooperation agreements, including joint product development agreements among small supply firms.

These government initiatives should help to encourage a supply chain that allows small firms to work together on contracts for the de-verticalized car manufacturers in the area.

(Source: Adapted from Morgan, K. (1994). "Reversing attrition: The auto cluster in Baden-Württemberg", Arbeitsbericht, Akademie für Technikfolgenabschätzung in Baden-Württemberg, No. 37.)

Annex 5

The Danish network programme

The proportion of the industrial workforce employed in small and medium-sized firms in Denmark is greater than in any other European nation. With the prospect of a more open European market, the small-firm sector was thought to be threatened by external competition from large firms to the point that its long-term survival was in doubt. The solution chosen is based on the idea that groups of small firms can compete with large enterprises if each specializes in only a few phases of the production process. In this way, the ensemble of firms reach a level of competitiveness comparable to that of larger firms. The Danish programme focuses on encouraging the creation of networks of small firms that can "compete successfully with the best of large companies" in terms of both scale and quality.

The programme promotes, with subsidies and advice, complementary activities among firms that could profit from the creation of a network: to share the fixed costs for a sales or buying department, to combine productive capacity, to share the expense of consultants or specialist training. In order to assure information transparency within the network, successful conflict resolution, and continuity in planning network activities, an innovative advisory system has been established. The Danish strategy aims to create a new class of professional brokers, trained through a scheduled programme. Some firms — several hundred — are stimulated by direct public financial help; the rest should be encouraged by successful examples to undertake similar experiences. In the long run, and given some spin-off effects, the hope is that this strategy will achieve not only changes in relations among firms but a more general transformation of perceptions of industrial production.

(Source: Adapted from Rosenfield, S.A. (1994). "Industrial strength strategies: Regional clusters and public policy", produced by Regional Technology Strategies Inc.)

Table 4. Strategies for supporting small businesses following privatization and restructuring

Strategy	Main actors	Examples	Indicators of success	Key success factors
Financial assistance: venture capital, credit guarantees and small business loans	Parent company; with support from local enterprise or development agencies. Sometimes part of the funding is provided by donor agencies	British Steel Industry (United Kingdom); British Coal Enterprise (United Kingdom); AAC venture capital fund (South Africa); Saint-Gobain Development (France); SOFREA (France); Pechiney (France)	3,500 businesses creating 58,000 jobs, with an 80% survival rate and 17 jobs per investment (British Steel); 5,000 businesses creating 55,000 jobs, with an 80% survival rate and 11 jobs per investment (British Coal); 300 SMEs created, employing 3,600 (AAC); 10,000 jobs created or saved from 500 investments (Saint-Gobain); 20,000 jobs from 830 investments (SOFREA)	Investment concentrated in area hit by job losses. Takes time for programme to gain experience in identifying potentially successful small businesses and entrepreneurs. Some (but not all) companies will not fund start-ups. Business advice and consultancy from local enterprise and development agencies important. Sometimes workspace provision is made available; where possible (see France) subcontracting and outsourcing agreements are important
	Donor agencies offering credit guarantees to participating banks or NGOs (for micro-businesses)	PBEP (Poland); Hungary	N/A	A sound banking system is essential. Takes time to develop trust between guarantee agency and banks; loan applications and guarantee claims should be processed speedily
	Multilateral and bilateral development banks extending lines of credit to commercial banks	EBRD's Russia Small Business Fund	Loan losses on micro-loans of 0.5%; 10,000 loans have been disbursed in three years (RSBF)	Efficient credit technology; swift and effective procedures for extending credit
Collaboration between large and small firms	Large company which provides assistance to local supplier firms, sometimes formed from ex-employees	ENI (Italy); AAC (South Africa); Philips, Siemens, Glyndia (India)	1,000 jobs created by 10 joint ventures between ENI and small firms. Also, seen as a means of creating acceptance of a large corporation within the local community	Financial services, technical support, management advice, space, equipment and subcontracting agreements to help small firms providing local employment, sometimes to ex-employees
Subcontracting exchanges	Chambers of commerce, business associations, government agencies	Genoa (Italy); France; Spain; Ireland; India; Philippines; Latin America; Morocco	N/A	Effective form of information flow on subcontractors and opportunities. Cooperation between groups of small firms can enable them to fulfil large subcontracts

Strategy	Main actors	Examples	Indicators of success	Key success factors
Management buy-outs	Management of parent company; venture capital investors; employee investors (in the case of ESOPs); lending banks	United States; United Kingdom; Romania; Hungary; former Soviet Union; South Africa	50% survival rate in the United States; 82% performed better than prior to MBO; employment reduction of 50% (United States) and 30% (United Kingdom) following MBO; ESOP firms grow faster than comparable US firms, and this growth creates 50% more jobs	Availability of venture capital as well as loans. Potential of exit options, such as stock market flotation; trade sale or refinancing
Spin-offs of separate sections of the parent enterprise	As for MBOs	As for MBOs	N/A	As for MBOs, though such large amounts of finance not always required. Also, the use of parent company assets, support and contracts are critical
Employment promotion companies	Restructuring company; trade unions; local and central government	EPQCs (Germany)	Important role in mitigating social cost of mass redundancies in East Germany	Huge level of public funding required to operate the EPQCs (very little private investment could be found)
Self-employment schemes	Government and local enterprise agencies; also outplacement agencies	United States; United Kingdom; Europe; Poland; Hungary	76% start-up plus re-employment rate (United States); 64% survival rate after three years, compared to 40% survival for all start-ups (United Kingdom); 76% survival after one year (United States); 70% survival after two years (United Kingdom outplacement agency)	Involvement of local enterprise agencies to screen out those unlikely to succeed, and provide technical and business advice. Also follow-up counselling based at the client's premises found to be helpful