FIRM UP PERFORMANCE

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From Capabilities to Opportunity: Driving SME Growth

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Addressing constraints to SME growth

• Most research focuses on supply-side constraints – capabilities
  – Entrepreneurship / management training: Do firm owners have the necessary skills?
  – Finance: Do firms have access to the capital needed for expansion?
  – Labor: Do firms have access to skilled labor?
Addressing constraints to SME growth

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"Luck is what happens when preparation meets opportunity."

Seneca
Addressing constraints to SME growth

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Demand-side constraints

• These supply-side constraints may be very important. But is addressing the supply side sufficient? Is it necessary?
• Maybe addressing the demand side is sufficient.
Providing a stimulus to demand: procurement

• Here’s a simple way to stimulate demand: The government is the single largest purchaser of goods in most countries.

• Ferraz et al (2016) is one of several recent projects that studies asking:

*Does winning a procurement auction stimulate growth for small firms.*

  – Other examples: Lee (2018); Alfaro-Arena et al (2019); Donaldson and Pomeranz
Providing a stimulus to demand: procurement

• Ferraz et al:
  – Not an RCT, but credible causal identification
  – Extensive use of administrative data

• Procurement auctions in Brazil have random ending times.

• Use the sample of auctions where there were at least 2 bids within the last 30 seconds.

• Compare winners and losers in these auctions.
Providing a stimulus to demand: procurement

• Outcomes:
  – Winning at least one bid increases growth one quarter later by 2.2 pp.
  – Effects are durable: Winners are more likely to bid in future auctions, and “excess” growth is sustained for at least two years.
  – Effects are larger for small, young firms.
    • Consistent with Haltiwanger et al(s) and Syverson suggesting that young firms are more constrained by demand.
Growth, but how?

• Procurement stimulates growth, but why? What do firms learn?
• Atkin et al (2018) provide nicely rich detail on the process. They use an export intervention among rug-makers in Egypt (Atkin et al, 2018)
• They linked with an NGO Aid to Artisans to establish links to export markets.
• Sample of 219 rug makers in Fowa, Egypt.
  – Production for the domestic market
Rugs and technology

Flat-weave “Dubs” Rug

Wooden Foot-Treadle Loom
Providing a direct link to new markets: Exporting in Egypt

• With help of Aid to Artisans, identified a local intermediary and – eventually – buyers for rugs.
  – Buyers in Germany, Israel, USA
Export markets
Providing a direct link to new markets: Exporting in Egypt

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• Randomly allocated the 219 producers to treatment and control. Gave production orders to the treatment weavers.

• A key point: The quality required for the export market is much higher than that required for the domestic market.

• The key question: Is there “learning by exporting”? 
  — Capabilities approach: Train the weavers to make higher quality products, then try to sell them in higher-income markets
  — Demand-side approach: “If you build it, they will come”
Export orders

Generating Export Orders

- Generating export orders was slow and difficult
- Failure is common in export markets; this is our 2nd location in Egypt
- 1/7 attempts lead to sustained exports (similar to Eaton et al 2013)
- Finally, obtained substantial and sustained orders in June 2012
- Orders come from high-income markets (US/Europe/Israel)
- Almost all orders are in one rug type (dubs)

Note: Slide from Atkin et al.
Did capabilities improve?

- Almost all firms (32 / 35) offered a “large” initial order accepted the export orders. Essentially all of them were able to deliver the product quality.

- Output – measured in square meters of carpets – decreased. And hours worked increased. But profits also increased.
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• After adjusting for product quality, output increased among the exporters
Why does quality improve?

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Why does quality improve?

• First, it does not improve immediately, though very quickly. There is a learning curve.
• Further evidence of learning: The “quality lab”
  – Atkin et al set up a shop and ask both treatment and control weavers to make a rug matching domestic standards.
  – In spite of there being no reward to quality, the treatment weavers produce higher quality.
• How do they learn? Evidence from emails suggests that the intermediary provides the training through feedback on the deliveries from the weavers.
• There is no evidence of actual investments, in equipment, consulting, etc.
Providing a direct link to new markets: Exporting in Egypt

• Almost all of a pool of existing small-scale manufacturers were able to transition to the higher quality standards required to produce products for export markets.

• Conclusion: Capabilities as “pushing the string.” The intermediaries increased the capabilities, but in a “learning by doing” fashion. The improvement in quality occurred quickly and without explicit investments.
Providing a direct link to new markets: Exporting in Egypt

• A nice example of demand inducing a change in capabilities.
• But Aid to Artisans says that around 6 of 7 such attempts fail. So what should we conclude about the policy lessons here?
Demand works, but does it lead to (aggregate) growth?

- These examples show that demand shocks stimulate changes in capabilities and growth.
- Does this add to aggregate growth, or just shift demand from one firm to another?
- The challenge is to use these projects to understand more about how markets function.
Jensen (2007) shows the arrival of mobile phones in Kerala, India changed the way fishermen sold their catch.
- Allowed them to check prices before coming ashore.
- Led to selling wherever the price was highest, rather than in their own village.

- Note that, unlike some of the studies I discuss, there is no administrative data available in this case.
Information, demand and markets

• Jensen and Miller notice that selling in other villages led fishermen to earn about the capabilities of boat builders in other places.
  – This led to a shift in demand from lower-quality (productivity) builders to higher-quality (productivity) builders.
  – The shift in demand led to economies of scale gains, increasing industry-wide productivity.
• Information, from the observed adoption of mobile phones, reduces frictions in the market.
Information, demand and markets

• Adrabi et al. conduct and RCT that increases information parents have about the quality of schools (majority private schools) in Pakistani villages.
  – Provide information about test scores and see how that affects behavior of schools.
  – The intervention does not change the capabilities of either schools or teachers.

• Question: Does the information on school quality induce underperforming schools to improve?
Pakistani school project design

• Sample of 112 villages; ~630 household per village
  • average of 8 primary schools per village
  • 166 children per village in school (grade 3)
  • Some government schools, some private schools
• Treatment at the village level. Outcomes?
The effect of information about quality

- Average school fees fall in treatment villages by 17%
- Enrollment increases by 3.2 percentage points in treatment villages
- Average test scores increase by 0.11 standard deviations in treatment villages (relative to control)
- Further evidence of market effects:
  - Scores improve most in the schools performing worst at baseline.
  - Investment in
  - Fees in the highest priced (and highest performing) schools fall.
Changing the “infrastructure” of markets

• The key point: The intervention was not designed to change capabilities directly. Yet product quality increased dramatically.

• Conclusion: Capabilities as “pushing the string.” The capabilities were there, but were dormant because the market did not provide the incentives to deploy them.
Last example: Reducing frictions, but not with information

- Higgins (2019) analyses the effect of rolling out debit cards to recipients of social programs in Mexico.
- A lot of the analysis focuses on technology adoption.
- I want to focus on the part that illuminates how the technology reduces frictions in the market.
- Prior to shifting social program payments to debit cards:
  - Large stores accepted credit / debit cards, “corner stores” did not
  - Richer households had cards, poorer households did not
Reducing frictions, but not with information

• Large increase in the number of debit cards in selected neighborhoods
  – This induced corner stores to adopt the ability to accept the cards
  – Now higher income households can use cards at corner stores as well as large stores

• Higher-income households shift purchases to corner stores

• Profits at corner stores increase
  – Mostly a shift in sales from large to small stores.
  – But because the adoption reduced a friction, likely increased aggregate welfare.
Concluding thoughts

• Demand can stimulate supply of capabilities. Changing the structure of opportunities and incentives appears to be more important in driving growth in many contexts.

• If the policy goal is aggregate growth, we need to understand how / why the intervention is improving the function of the market, for example, by reducing information frictions.
Thank you!