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The Impact of Adjustment Policies on Microenterprises

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Introduction

The discovery of the importance of micro-enterprises and the dynamics of the informal sector dates from before the economic and financial crisis and the implementation of adjustment policies of the early eighties. Still, these policies brought out and accentuated the strategic importance of micro-enterprises, on the level of the production of goods and services providing essential needs, as well as that of the income distributed, jobs created, or training and qualifications acquired.

The purpose of this paper is to analyze certain effects of adjustment policies implemented in developing countries on the informal sector and micro-enterprises. This requires that the object and methods chosen first be defined:

1/ All terms must be explained.

- The definition of the informal sector or the micro-enterprise has been the subject of debate for nearly 20 years<sup>1</sup>. The statistical definition distinguishes an outlaw sector (the absence of data processing, failure to comply with applicable codes and fiscal policy, limited turnover or number of workers). A functional definition makes use of organizational criteria: "small-scale activities in which the body of wage earners is limited, in which a small amount of capital is put forth, but in which monetary circulation and the production of goods and services nonetheless occur for valuable consideration." Certain distinguishing characteristics can be retained: flexibility, few barriers to entry, limited capital intensity. The criteria most often accepted since the Kenya report (1972) are easy access to activities, the use of local resources, family ownership of enterprises, small-scale operations, highly labor-intensive and adapted technologies, qualifications acquired outside of the official educational system, markets escaping any regulation, and openness to competition.

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<sup>1</sup>Cf. Hugon (1980), Deble, Hugon (1982), Penouil Lachaud (1985), Archambault, Greffe (1984), Sethuraman (1976).

- Adjustment has become a polysemous term, sometimes used in the sense of stabilization or, on the contrary, referring to growth-sustaining structural changes. In the broad sense, it can be defined as the process by which an economy adapts to the international environment, or, more specifically, as the manner in which the balance of payments reaches equilibrium after a disturbance; in the strict sense, it is distinguished from stabilization (restriction of overall demand), and corresponds to an increase in production, to a promotion of exports or a process of import substitution. Structural adjustment can be defined as follows: "the durable adjustment of the balance of payments obtained through an adaptation of economic structures (principally productive structures, i.e., other than through reduced economic growth, or increased or excessive recourse to outside capital<sup>2</sup>. The implementation of adjustment policies is ensured by structural adjustment loans (PAS) or sectorial loans: "loans granted for the purpose of sustaining a profound reform in policies and institutions in developing countries to allow the latter to bring current account deficits to more tolerable levels in the short run, while maintaining the greatest possible effort for development"<sup>3</sup>. Compared to projects, PAS are characterized by specific traits: rapid disbursement, macro nature, non-assignment, relationship with economic policy program implementation (conditionality).

2/ Three major methodological difficulties are encountered in the study of the impact of adjustment policies on micro-enterprises:

- A problem of information: despite several recent World Bank and UNICEF studies (1987) and research programs conducted by the OECD Development Center (1987-89), and the BIT [International Bureau of Labor], information systems are very poor (Pfefferman, 1987) in terms of identifying the scattered effects of adjustment programs. These systems make reference to macroeconomic indicators and standard models designed within Keynesian contexts of national accounting equilibria and aggregates, or the monetarist framework of monetary-financial equilibria, which exclude social indicators (nutritional evaluations, jobs, income, medical condition or educational status), as well as organizational and management indices, social structures and the process of redistribution. Available studies on the informal sector provide results in instantaneous sections that do not allow the link between micro-enterprises and adjustment dynamics to be established.

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<sup>2</sup>Guillaumont (1986).

<sup>3</sup>World Bank (1986).

- A problem of defining adjustments in time and space. Adjustment is a process, the effects of which extend over several periods; there are social transition costs, there is a response to current account disequilibria, and, most often, to economic and financial crises. Hence, it is important to make a clear distinction: the structural or cyclical origins of economic and financial disequilibria, the manifestations of disequilibria at the domestic or foreign level, stabilization measures aiming to reduce overall demand; adjustment measures aiming towards restructuring the economy and reallocating resources, and adjustment loans allowing access to foreign credits. Monetary and fiscal policies generate contraction in demand or domestic credit in the short run; other measures, aiming to change the structure of expenditures and to reallocate resources, only exert their effects in the medium term, while organizational and institutional reforms can be placed in the long term horizon.

- A problem of attribution. It is a question of attributing certain effects to adjustment policies. In the absence of experimentation which is impossible in the social sciences, three methods are generally used: comparing the situations in the countries depending on whether or not they have adopted adjustment policies; studying the evolution of economies before and after adjustment programs; evaluating divergences between the objectives set forth and the results obtained. We shall retain the latter method.

In this paper, we will distinguish the following:

- I - The dynamics of micro-enterprises and the informal sector
- II - The effects of adjustment policies on these dynamics.

#### I - THE DYNAMICS OF MICRO-ENTERPRISES

The discovery of the dynamics of micro-enterprises and the use of the term "non-structured" or "informal" sector in less developed countries result from the understanding of three phenomena, the coexistence of which is a priori paradoxical:

- The urban explosion has occurred at an accelerated rate during the past three decades: while the populations of countries having per capita incomes under \$ 1,000 increased at a rate of approximately 2.4%, the urban population increased over 6%, while the population living in shanty towns or peripheral zones grew an average of over 12% per year.

- Average economic growth, relatively strong during the seventies (with major divergences between countries) has dropped dramatically since 1980; on the whole, this was achieved through the use of highly capital-intensive technologies and increased productivity, which generally had direct negative effects on

wage-earning labor<sup>4</sup>. Industry not only materialized as the result of import substitution, but through competition with respect to local small-scale production operations. It was financed in part by a surplus drawn down from the rural world, and was often a factor in the latter's regression. Thus, economic growth exerted the effects of increasing labor capacity supply, to a greater extent than the effects of increased demand. Even in countries experiencing relatively rapid growth rates, there was generally a decrease in wage-earning jobs as a percentage of the active population. The absorption of workers by the development of the modern sector appears illusory for countries experiencing demographic growth rates in excess of 2.5%. For the new arrivals on the labor market to be integrated into the modern sector, wage-earning jobs should represent half of the active population, while, in most less developed countries, the percentage ranges from 10 to 20.

- However, despite the gap between supply and demand for labor, apparent or disguised unemployment has not increased as quickly as the rate of the rural exodus would imply. Thus, it must be explained how the unemployed can subsist in the cities; traditional explanations involving parasitism (a worker supporting non-workers), or by transfers from the country to the city, have generally been disproved. It has become apparent, and BIT experts have contributed to the disclosure of this phenomenon, that there existed a little-known non-structured, or informal sector, which played an essential role in the absorption of migrants (transitional sector), the creation of jobs and the circulation of real and financial flows in the cities. Studies conducted since 1969, especially within the context of the BIT World Employment Program<sup>5</sup> estimate that the activities of this non-structured sector represent between 20 and 30% of the jobs in Third World cities.

The Non-structured/structured sector dualism constituted a new way to evaluate the heterogeneity in the structures of less-developed economies: beside the capitalist sector (wage-earners, positive profit rate, money functioning as capital) and

<sup>4</sup>The wage-earning job index has increased slightly since 1950, though with significant differences depending on the city. Thus, in French-speaking Africa, the only cities in which wage-earning jobs increased significantly are Abidjan, Brazzaville, Pointe-Noire, Nouakchett and Libreville. According to BIT, urban unemployment and underemployment affected over 35% of the African population in 1980.

<sup>5</sup>The adoption of the BIT World Employment Program gave veritable impetus to research focusing on revenues, poverty and informal employment (studies on urbanization, expert reports and studies on the non-structured sector).

the non-commercial space (absence of monetary circulation, production of simple consumption goods, self-subsistence), a complex of activities that we can classify into an "informal" or "non-structured" sector, not from the aspect of consumption goods provided, but based on the forms in which production, socio-professional statutes or division of labor are organized.

The dualistic analysis have thus been reversed: instead of considering the traditional sector as having a passive role supplying labor at low wage rates determined by the subsistence income<sup>6</sup>, it is analyzed by virtue of its dynamism properly speaking, and its positive role.

The new growth models have adopted the assumption that income inequalities were not a factor in the redemption of savings, a source of investment, but, on the contrary, limited effective demand. The question at hand at the level of employment thus concerns income and not only labor time, while the economic problem has moved from production to demand.

#### I.1. - The results of surveys?

Over the past fifteen years, various surveys have been conducted on micro-enterprises in major Third World cities, either under BIT impetus, or that of national or university research organizations. These investigations define an informal sector based on certain criteria (size, turnover, number of workers, absence of accounting, etc.) and aim to quantify their mode of operation according to an economic analysis grid (jobs, gross operating results, input productivity). On the contrary,

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<sup>6</sup>According to the authors, the traditional sector (subsistence, precapitalistic), encompasses different realities and different sectors; in many models, it is assimilated with home-consumption agriculture. Conversely, the Lewis model includes in the subsistence sector traditional agriculture, domestic services and minor urban trades; it defines the subsistence sector as the absence of reproducible capital. Two different cases can be considered to explain wage determination: the one envisioned by Lewis, in which, in a neo-classical scope, the subsistence sector merely provides workers and exerts pressure on the labor market at the level of labor supply; that of the classical models, in which the subsistence sector will exert upward pressure on wages in the capitalist sector (making labor supply scarce); in the second case, it will, on the other hand, exert downward pressure on real salaries.

<sup>7</sup>Cf. Bose (1974), Bromley, Gerry (1978), Charmes (1985-1986 - 1987), Hallack, Caillods (1981), Joshi, Lubell Mouly (1976), Lachaud (1976 - 1981 - 1982), Maldonado (1988), De Miras (1980), Sethuraman (1988), Van Dijk (1976 - 1980).

other studies involve the methods for allocating labor among the domestic, commercial, capitalist and government spheres, in relation with the social structure and the forms of power peculiar to each society, and avoid heavy, universal and quantitative questionnaires.

The surveys show that small urban activities, far from disappearing, are in full expansion and that they account for the majority of urban jobs, providing goods and services essential for the lifestyles of the agents, and distributing revenues higher than those found in the rural world, and often comparable to those in the modern sector.

The dynamics of small urban activities is thus essential in understanding the self-sustained process of urban growth and the maintenance of a certain standard of living in the urban areas despite the crisis the modern sector is experiencing in many countries.

#### I.1.1. The principal characteristics of micro-enterprises

We cannot summarize the results of these studies here, but can extract a few of their general characteristics: young operation heads, low barriers for entering the industry in terms of investments, which are generally provided through personal savings; the use of simple technologies, and non-wage social relations. The absence of accounting, the small degree of differentiation between the production unit and the domestic unit make it impossible to assume that the maximization of gross operating results is the primary objective. There is generally a risk-minimization strategy in an aleatory universe, and the goal of diversifying activities for those generating surpluses. At the level of outlets, small-scale production, having non-credit-worthy and very unstable demand, generates a high degree of divisibility and fragmentation of goods and services with respect to a personalized clientele. If these activities function outside of official regulations, they are highly structured at the organizational level, relying on family, ethnic, cast or corporate relations, depending on the case.

The principal industries involved correspond to fundamental needs: housing, transportation, clothing, food.

Certain trades can appear as urban vestiges of traditional activities, but most correspond to modern creations related to new problems, even if they do rely heavily on old social structures and family relations. They often constitute forms of social experimentation or resistance to power.

Most urban people, i.e., those who do not have access to industrial merchandise or community services, are producers and consumers of these "informal" activities. The latter range from

commercial services rendered to persons, or goods, to small-scale production operations, by way of industrial product collection and recycling activities, and small intermediary activities in trade and transportation. These activities function in the margin of legality; if certain are illegal, most of them are "a-legal" and are tolerated by the public authorities. The predominant characteristics of these activities are that they go beyond the reach of the taxation system, operate outside of corporate regulations, are managed with no accounting system and are based on labor organizations with no dominant wage-earning structure.

If these activities are concealed at the level of accounting methods, they are still obviously visible. A European living in Africa knows that the small clandestine garage will supply him with the spare parts he needs, or that, in Lagos, if the photocopy machines at the ministries break down, one can always use street photocopy machines run by individual electric generators. Unofficial activities are part of daily life for Third World citizens.

The consideration of these activities makes it possible to explain numerous hidden phenomena through approaches in terms of economic development, national accounting and macro-economic aggregate indicators.

#### I.1.2. - The operation of the "non-structured modern sector"

Because of the heterogeneity of the objectives and methods, many questions remain as to the meaning of results. We will distinguish four main questions on this subject.

- What are the relationships between small production units and the modern sector? - Several levels can be distinguished in order to understand these relations: workers, goods, credits, outlets, prices.

Whereas industrial subcontracting in Southeast Asian port cities leads to connection between small production units and major firms, this form of integration seems virtually non-existent in Sub-Saharan Africa.

- Most studies seem to confirm the absence or weakness of relations between methods of financing, outlets or workers and the modern sector. Most of the capital comes from personal or family savings; downstream relations are very limited. On the other hand, upstream dependence appears to be great, from the aspect of fixed capital as well as that of raw materials. Other forms of relations or dependencies are observed: the case of small-scale producers, which are formally independent, but which depend on traders to supply them with raw materials, credit and

outlets; the case of small producers whose capital in fact belongs to employees, or who are dependent on their customers.

- Another question involves the establishment of prices. Most inputs come not from the rural world (except in agro-food), but from the modern sector, and their prices are reflected in production costs; transmitted inflation is present. On the other hand, knowing whether or not prices for goods and services provided by small units are lower than modern sector prices raises a question stemming from problems of comparison: cigarettes sold on a unit basis by a retailer without a site cost more than those sold by the package in a supermarket. Small producer prices are generally much lower than modern sector prices. For example, "Ho Chi Minh shoes" are less expensive than "Bata" shoes, or semi-clandestine transport competing with official transport).

Above and beyond these factual examples, the questions concern whether or not consumption goods markets segmented according to social groups exist, whether or not competition exists between small and large unit prices, the effects of domestic or imported inflation on the prices of small producer goods and services, the role of bargaining in the establishment of prices. Does the existence of small-scale trades allow pressure on wages, or, in other terms, does it "downgrade the work force?"

Is accumulation possible for micro-enterprises? - In most studies, opposition is found between an involutive informal sector and an evolutive or transitional informal sector (Jean-Fierre Lachaud), a subsistence and transition sector (Jacques Charmes and Claude de Miras); a residual and intermediary sector (William Steel) or a non-structured traditional and modern sector (Georges Nihan); the criteria do not fully overlap, but do go back to a distinction between the units generating a surplus for accumulation purposes and those which do not. Still, there is a contradiction between the results of surveys showing that there is no gradual development, that the surplus is minute, that there is a great deal of competition at the level of supply, which exerts pressure on prices, and thus the process of the development in the sector is involutive, and work which, on the other hand, involves possibilities of accumulation.

Thus, several studies based on factorial analysis note the positive relations between the level of investments, raw materials, and revenues. On the other hand, in a comparative study of Freetown, Lagos, Bamako, Kigali, Lomé and Nouakchott (1980), Georges Nihan shows that the rates of return on capital are lower for more capital-intensive units. Based on the study of the production function of the small firm, "the cornerstone of any study of economic potential and employment in the non-structured sector," the decile study shows that labor

productivity does not increase along with investment in sufficient proportions to compensate for the decrease in capital productivity. The author advances as an explanatory hypothesis the existence of diminishing returns, incompetent management or labor having qualification levels unsuited to the level of technology ... Returns on capital were thus higher in labor-intensive production units" ... The author does not delve into the fundamental point of knowing whether or not these results are related to economic behavior (non-maximization of profits, the absence of accounting) or to structural facts (small influence of competition). Regardless of the terminological or doctrinal debates, these results pose a problem with respect to common sense reflections on the limits to accumulation.

The studies thus yield divergent results on questions such as: Does gradual development occur, or do units that accumulate do so through an external process? (the example of employees who invest in small-scale production). Can difficulties in accumulation be explained by outside factors (price policy, credit or protected markets), or by internal factors within the industry? Especially: Can the refusal of credit be attributed to the small owner's desire not to engage in labor organization? Substitution among apprentices and employees is impossible, even if it appears to be economically profitable, quite simply because it would involve a change of social production relationships. On the whole, these studies, which are devoted to the upper part of the range, reveal the existence of a positive surplus and capacities to accumulate up to a certain threshold. It seems that, beyond this threshold, the formation of capital-intensive units results from voluntarist action on the part of the Government, outside of the industry.

- Are jobs created? - small-scale activities absorb the uneducated or the "de-educated," migrants, the unemployed, workers rejected by the modern sector or seeking higher incomes. In this respect, various studies also provide significant figures which reveal the essential role informal activities play in the volume of urban jobs created (generally over 20% of the active urban population). However, this result does not make it possible to gain much further knowledge; on the one hand, because it is trivial to show that there is a good relationship between activities defined a priori by their low labor productivity and the volume of labor hours; on the other hand, because the term of employment, which itself is very ambiguous, conceals the heterogeneous nature of labor statutes and labor markets in the cities.

- What are distributed revenues? - Studies reveal that entrepreneurs generally have higher incomes, or incomes at least equal to, the minimum wage (80% in Nihan's modern SNS sample); on the other hand, worker income in this category is lower than minimum wage. An essential question is that of apprenticeship;

all studies show that apprentices have very low incomes. However, the question concerning the contribution of apprenticeship to production (unpaid work force) and training (acquisition of human capital) is not addressed in our opinion, even if studies reveal a positive relationship between income, on-the-job training, and the greater efficiency of this method over professional training. Certain work has shown that apprentices are extremely young, and regard this as a method to gain experience leading subsequently to the owner position; on the other hand, other studies regard apprenticeship as a way to extort excess labor because of the virtual gratuity of the work force, and insist on low wages; the results of surveys show the essential role of the family in understanding the owner/apprentice relationship; it is found beyond the realm of the law, with an ethnic identity between owner and apprentice, and duplication of the elder/younger division. Finally, according to Charmes, to sustain itself, small-scale production is making the weapons of its dissolution: facing competition from high-productivity units, small-scale production shops reduce their costs, extend apprenticeship periods and limit the number of apprentices. The latter are unable to find jobs, thus clandestine shops multiply, entering the industry and competing with the former.

#### I.2. - Analysis: trialist models

All of these results can be systematized into a trialist model, which distinguishes a subsistence sector (traditional or marginal), a transitional sector (intermediary or non-structured modern) and a capitalist sector<sup>8</sup>.

- The first sector, which plays the role of absorbing excess labor, has an average productivity corresponding to the minimum for subsistence, and thus cannot generate the surplus necessary for accumulation.

- The second sector, with low capital intensity, is characterized by the absence of permanent wage earners and labor relation codes, precariousness and use of specific social relations allowing virtually cost-free or poorly-paid work, and a mode of competitive regulation largely escaping government control.

- The third sector, highly capital-intensive, is defined by wage earners, labor relations codes, the existence of

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<sup>8</sup>We refer the reader to the study we conducted on "La petite production marchande et l'emploi dans le secteur informel" [Small Commercial Production and Employment in the Informal Sector" (1976) in the special issue of Revue Tiers-Monde no. 82, 1980, and the work prepared in cooperation with Isabelle Deble (1982).

administered prices, the importance of a variety of Government protection and subsidies, and a monopolistic mode of regulation. However, considering the size of the markets and the scales of production, the small capacity for technological control, the absence of industrial substance, fluctuations in demand, the freeze of capital and effective differences in labor compensation, "natural profit rates," in the absence of Government intervention, are generally greater in the second sector.

These paradoxical results are found empirically in the various studies devoted to the "modern non-structured sector." The increased labor productivity resulting from increased capital intensity is insufficient to compensate beyond a certain threshold for the decrease in apparent capital productivity. There would exist a technological threshold leading to decreasing financial returns; this can be explained by technical constraints, management difficulties or by relations between the technology used and the organization of labor<sup>9</sup>.

Thus, we can synthesize the reasoning as follows<sup>10</sup>:

- The capitalist sector (1), oligopolistic, is highly capital-intensive ( $k$ ), with a high marginal productivity level for the value of labor ( $q_m$ ), with institutional wages clearly greater than subsistence income ( $w_1$ ); it has access to institutionalized credit at preferential rates. Considering the price of inputs, this sector, having a high technological level, tends to create few jobs. It is assumed not to have intersectorial relations with the other industries, but competes with them at the market level.

- The intermediary sector (2) has a low degree of capital intensity; the existence of barriers to entry (human or financial capital) lead to a high positive marginal productivity of labor, despite stiff supply competition. Exogenous and constant labor revenues are defined by the minimum for subsistence. In this sector, there is an unlimited supply of labor at subsistence-level income. Employment is defined by the equalization of marginal productivity in value ( $q_m$ ) and labor revenues ( $w_2 = w$ ). We assume a production function having substitutable inputs.

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<sup>9</sup>Various work by the BIT in the modern non-structured sector, especially Nihan in Hugon, 1980.

<sup>10</sup>Trisectorial models generally involve only the urban space. However, using the Lewis hypothesis, we can consider that the subsistence sector involves at once subsistence agriculture and small urban trades, while the intermediary and capitalist sector involves the industrial sector as well as tent crop agriculture.

Considering the non-linear relationship between labor productivity ( $q$ ) and capital intensity ( $k$ )  $q = F(k)$ ; there exists a level of  $q(q_0)$  and  $k(k_0)$  at which the rate of return on capital is maximized  $j = \frac{q - \bar{w}}{k}$ . The rate of accumulation depends on the profit reinvestment rate. It is assumed that there is no technological progress involved.

- The subsistence sector (3) can be defined by the absence of reproducible capital. There are no barriers to entry. Subsistence income ( $w_3 = \bar{w}$ ) is equal to average labor productivity. Employment volume is determined by the level of demand. This sector is merely a "sponge" which absorbs surplus labor.

The strategy consisting of relying on the intermediary sector can, under certain conditions, ensure at once the fastest rate of accumulation and the highest growth of employment over time. If we assume that the rate of return for sector (2) is fully reinvested, product and employment in sector (2) increase exponentially at the rate determined by  $j$ . The optimal strategy consists of eliminating the advantages of the oligopclistic sector (protected markets, low-priced financial capital) and allowing the laws of supply and demand to come into play for the intermediary sector (subsistence wages, credit subject to payment).

We can show the operation of the three sectors using a four-quadrant graph:

- In quadrant (I), the production functions indicate the relationships between labor productivity ( $q$ ) and capital intensity ( $k$ ) for sectors 1 and 2; considering the exogenous determination of income ( $w_1$ ) and ( $w_2$ ), we obtain the respective levels  $k_1, k_2, q_1, q_2$ ; surpluses per worker are equal to  $q_1 w_1$  and  $q_2 w_2$ .

- In quadrant (II), considering both labor supply curves and both marginal productivity of labor curves in sectors 1 and 2, the respective employment levels are  $OL_1$  and  $OL_2$ . Moreover, sector 3 has an employment level of  $OL_3$ . Total wage bills are respectively  $OL_1 A_1 w_1, OL_2 A_2 w_2$  and  $OL_3 A_3 w_2$ . Profits are  $w_1 A_1 B_1 q_1, w_2 A_2 B_2 q_2$  and 0.

Quadrant (IV) shows the capital used in each sector  $OL_1 C_1 k_1, OL_2, C_2 k_2$  and 0.

- Dynamically, profit reinvestment (II) moves the marginal productivity of labor curve to the left of  $q_{m1}, q'_m1$  and  $q_{m2}, q'_m2$ ;  $k$  and  $q(I)$  remain the same; if all profit is accumulated:



1) If we assume that differences in capital intensity between the two sectors 1 and 2 are greater than the differences in surpluses generated per worker, rates of return are greater in the intermediary sector:  $j_1 < j_2$ ;

2) If we assume that the differences in employment volume between the two sectors are greater than the differences in surplus generated per worker, total profits are greater in the intermediary sector:

$$M_1 = (q_1 - w_1) \cdot L_1 < M_2 = (q_2 - w_2) \cdot L_2 ;$$

3) If profits are accumulated according to proportion  $a$ , the rate of accumulation and the rate of job creation are greater in the intermediary sector if:

$$a_1 j_1 < a_2 j_2$$

$$g_2 > g_1 \text{ where } g_1 = \frac{\Delta L}{L} \quad \frac{\Delta K}{K} = \text{a.s.}$$

These results weaken those of Sen/Emmanuel-type models, which chiefly assume a homogeneity of the labor market and establish a positive relationship between capital intensity and labor productivity. In a liberal interpretation, the dynamics of the intermediary sector and the subsistence sector is a response on the one hand to the non-competitive nature of the highly capital-intensive sectors and, on the other hand, to the distortions resulting from the burden of the State. Because of structural inflexibility, social protection and monopolies, which prevent the official sector from adapting to social pressures, society found ways to regulate demographic pressure going from primitive capitalism to the system D of modes of living and survival in urban surroundings.

To foster the intermediary sector, it is thus recommended to return to the laws of the market at the level of compensation for productive inputs, and to reduce protection and subsidies allowing the monopolistic sector to fight against "primitive competition" from intermediary activities. For the subsistence sector to play its role as a regulator of demographic pressure, it is important for the Government not to intervene, and to tolerate a-legal or outlaw activities.

The effectiveness of adjustment policies is directly related to the pertinence of these dualistic or trialistic hypotheses, and to the possibilities of substitution between the major unit and micro-enterprise sectors.

## II - ADJUSTMENT AND EFFECTS ON MICRO-ENTERPRISES

Adjustment policies implemented since the beginning of the eighties have the primary objective of promoting the substitution

of large protected organizations with small competitive entities. They theoretically aim to modify the economic structures in order to re-establish domestic balance of payment and financial equilibria and, beyond this, to restructure the economic composition to allow it to return to a path of growth without imbalances. If demand management is the prerequisite, it is accompanied by measures to restructure supply using action on prices, but also on sectorial management methods or actions.

In the background, economic reorganization, liberalization, changes in the pricing system involve modifications in the social structures and relationships of power between groups connected with foreign relations and those involved with domestic relations, between the rural world and the urban world, between the public sector and the private sector. The liberal project aims to bring out the innovative actors and to break excess profits, to reduce black markets and to introduce efficiency and streamlining into resource management.

#### II.1. The projected effects of adjustment policies

The priority goal of adjustment measures is to re-establish balance of payment equilibria, and, beyond this, to ensure conditions of growth.

- Disequilibria are essentially explained by excess demand over supply, because of discriminatory measures, both domestic (administered prices, subsidies) and foreign (excessively high exchange rates, exchange controls, protectionism); non-tradable sectors are thus given precedence over tradable ones; public expenditures exert crowding-out effects on the private sector, redistributive objectives override productive logics.

Hence, the principal adjustment measures involve the following:

- Opening onto the world market: this is based on the liberal principles of comparative advantage, the free circulation of inputs, exchange rate equilibrium. The relaxing of exchange rates, reduction of actual protective measures reconciled with nominal protective measures, the absence of non-tariff protection (with the exception of the rationing of some strategic products), and the re-adjustment of monetary parities constitute complementary measures, should prevent sectorial distortions, and shift the terms of trade and productive resources from non-tradable sectors to tradable sectors.

- Domestic liberalization: the principal institutional reforms aiming to return to the "laws of the market" involve the liberalization of trade, the reduction of the role of Government, trimming the fat off of public and para-public companies, recourse to privatization; deregulation must lead to the

dismantling of protective measures, subsidies and stabilization organizations; streamlining and privatization of the public sector must allow greater efficiency and eliminate the crowding-out effects of the public with respect to the private sector.

- The decrease and reorganization of expenditures: the decrease in the absorption (real flow perspective), or of domestic credit (monetarist perspective) must re-establish balance of foreign accounts equilibrium at the expense of domestic balance. It must also involve a reallocation of expenditures; a decrease in the production of protected sectors and an increase in that of the exporting sector. This restructuring of demand by overall macro and sectorial measures goes along with assigned loans to rebuild tradable sectors (structural adjustment loans). Thus, the increase in agricultural prices is assumed to effect a transfer of revenues from the city towards the rural world and foster an exportable surplus. The emphasis is also placed on the fight against poverty and the problems of income redistribution. As a complement to the correction of financial disequilibria, growth must result from an increase in overall capital flows, public and private. The coordination of financial backers and the generalization of aid flows must especially allow a positive flow of transfers to be maintained between each country.

All of these measures combined are assumed to reduce excess profits and protection of certain privileged groups (excessive profits based on foreign trade, subventions to protected groups: the educated, employees, military personnel, urban wage earners); it must foster the emergence of the innovative actors of civil society. To the extent where public expenditures tended to favorize the middle classes (cf. Pfefferman, 1987), the decrease in these expenditures should affect this level as a priority.

The revaluation of agricultural prices, reorganization of industries through structural adjustment loans, provisional rationing at the level of food imports and elimination of consumer subsidies must lead to a reallocation of resources from agriculture and the urban world towards the rural world (changes in the terms of trade).

The measures aim to reduce income related to the Government machinery and to encourage innovative groups to emerge at the level of the private and informal sectors. The model is that of medium producers (green revolution farmers or small to medium-size companies [PMEs]).

## II.2. Adjustment and micro-enterprises

Adjustment policies tend to bring about truth in prices, merchandise and production inputs, leading to a substitution from large units towards small ones. These policies act indirectly on

small enterprises, eliminating the advantages of the large units (subsidies, negative real interest rates, excessively high exchange rates, public contracts, etc.). They act directly by liberalizing the markets and modifying relative input prices.

The issue is obviously one of validity, viscosity, flexibility and substitutability. On the other hand, adjustment policies can have regressive effects on micro-enterprises, by reducing solvent demand, or limiting inputs and equipment goods imported or provided by the modern sector.

If we take as a criterion the tradable or non-tradable nature of goods and services and the wage or non-wage organization of labor, it is possible to define four groups (domestic or associative, small commercial production, government and capitalistic). Each of these groups has relations of trade, dependence, integration with the others and also possesses relatively autonomous dynamics. The question thus pertains to the effects of adjustment policies on each group; if we assume that each one is relatively autonomous and conducts balanced trade with the others, effects of substitution appear; on the contrary, relations of quasi-integration, subordination lead to relations of complementarity.

Several studies on the "informal" sector in Latin America (cf. Lautier, 1988) show that the effects of substitutability are limited, the low cost of labor (considering productivity) and flexibility of compensation do not seem significant. The dynamics of the "informal" sector, significant in periods of growth, appears more limited in times of recession, except for the most marginal activities.

Of course, it is possible to respond at a general level on relations peculiar to each society. From a logical perspective, several opposing effects can be noted:

- The truth of prices can promote a transfer from the government sphere towards the capitalist or the simple commercial sphere, but can also lead to market exclusion (cf. the SEN model<sup>11</sup> reinforcing the domestic sphere;

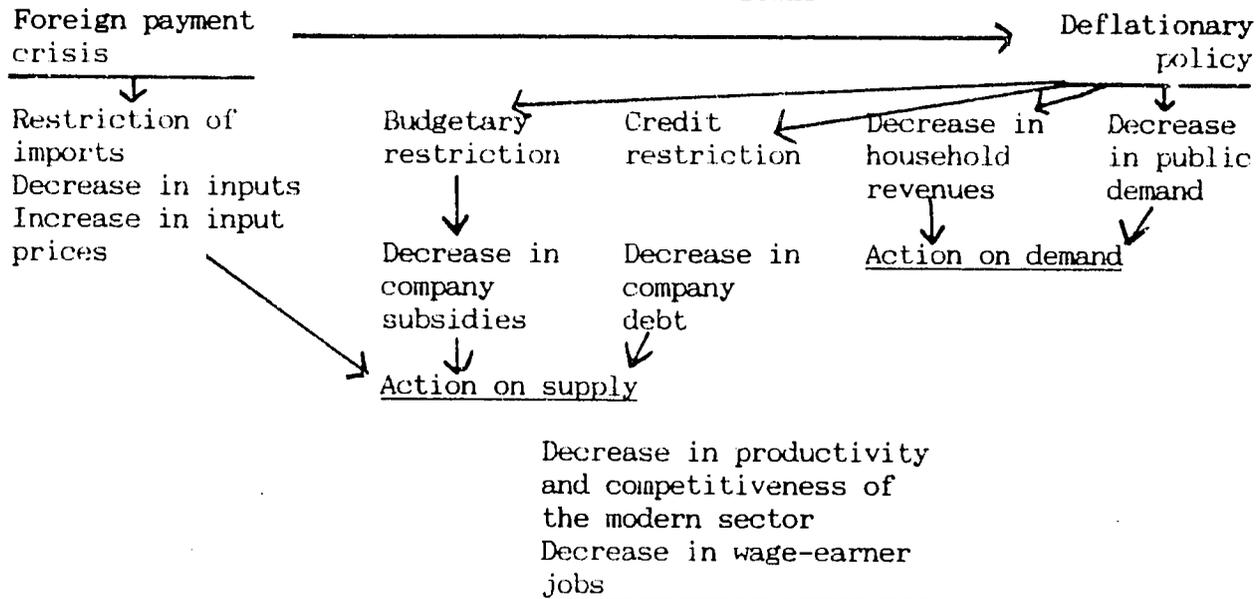
- The decrease in salaries and public consumption can create dynamics of substitution at the level of commercial activities, but can also generate recessionary effects (the Keynesian multiplier playing upon the decrease in the level of demand, or the effects of the decrease in inputs and imported equipment on activities).

The diagram below summaries some of these effects:

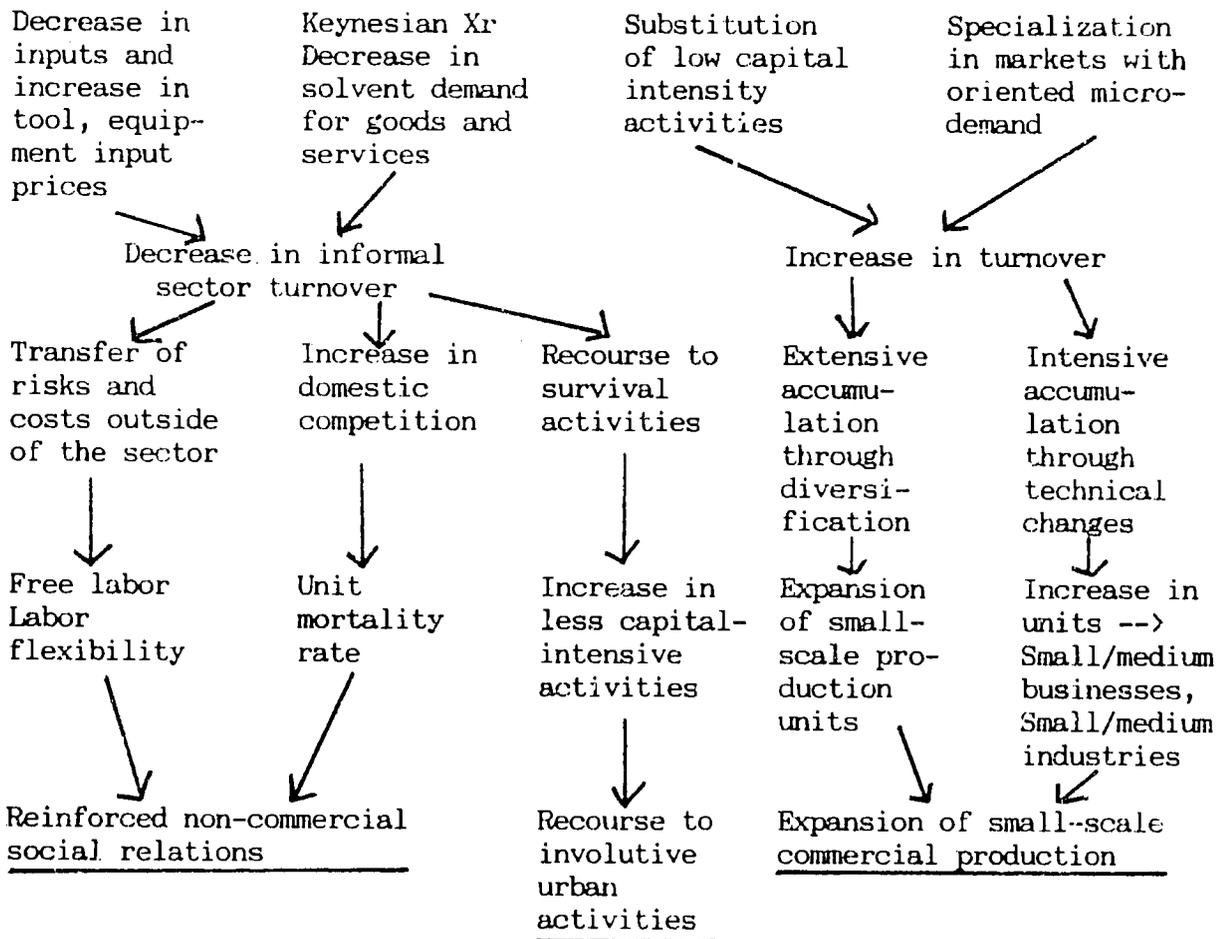
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<sup>11</sup>SEN (1981).

THE EFFECTS OF CRISIS AND ADJUSTMENT POLICIES  
ON "INFORMAL" ACTIVITIES



Effects of complementarity ← → Effects of Substitution



Urban emigration  
Swinging migrations  
Elimination of marginal elements

Urban Pauperization

## II.3. - Economic policy debates

### II.3.1. - Substitutability versus complementarity

According to the partisans of flexibility of the informal sector, micro-enterprises would play a role of substituting informal industrial with formal industrial jobs, or tertiary informal jobs with industrial jobs. Several authors emphasize the "possibilities offered by the non-structured sector for reducing unemployment and poverty" and see in this sector a "spontaneous and creative popular response to the State's inability to meet the most elementary needs of the poor (Vargas Llosa). For certain liberals, small enterprises would stem from unsuspected capacities for generating jobs and wealth; their productivity in the area of services, construction, even industry, is considerable compared to the inefficiency of large organizations; their capacity to create jobs and adapt to the unknowns of the market is great because of their informal nature, their low wage and social burdens. For other authors (cf. Cornia in L'ajustement à visage humain), under certain conditions, the non-structured sector can be a substitute for the industrial sector; competing against it in several markets, in situations of decreasing income and difficulty in the industrial sector, the non-structured sector profits from cost and price flexibility.

On the contrary, according to the partisans of complementarity, the informal sector has a dynamic largely induced by real demand and connections with the modern sector. Supply substitution involves only a limited fringe of markets, and has little to do with industry. Labor productivity-compensation ratios for labor are close. While, during periods of expansion, we see the development of micro-industries generated by the modern sector, phases of depression are, on the contrary, characterized by an increase in the most marginal activities (micro-trade or micro-service). Complementarities appear at the level of real demand, inter-sectorial connections, subcontracting relationships. According to Lautier, "The flexibility of real non-wage compensation does not cause the informal sector to create industrial jobs that the formal sector loses in recessionary phases and as the result of adjustment policies."

### II.3.2. - Internal or environmental disadvantages?

Divergences on the assessment of results generate different opinions on strategies to correct them. For some, the disadvantages of the non-structured sector would be inherent in small-scale activities (low productivity, inappropriate technology, primitive competition) and aside from a few specific units, this sector would be doomed to stagnation in the event of economic development. Conversely, other authors have

demonstrated the structural disadvantages attributed to the failure to respect the laws of competition and the advantages given to major enterprises (protectionist rights for substitution industries, tax exemptions, investment codes, advantageous interest rates, licensing programs, etc.). The problems of the non-structured sector would stem from the fact that the enterprises operate in the margin of the aid system and Government regulations, and have no access to credit institutions or modern technologies.

For the first, "the laws of the market" must be allowed to come into play, not favoring small-scale, low-productivity activities. The second, on the contrary, propose the priority development of the "non-structured" sector, which would generate revenues under the multiplier effects of jobs, which would employ workers skilled though having limited educations, using "soft" and "adapted" technologies.

### II.3.3. - Employment or productivity?

For some, the objective is no longer to maximize production, but, as a priority, to increase employment. The fight against unemployment and the fight against poverty become indissociable: the redistribution of income, the satisfaction of essential needs are the necessary components of this new strategy. In the more inward-looking model, putting a stop to the pauperization of farmers makes it possible to limit the rural exodus and to provide the necessary labor for agro-industries, and induces demand exerting the same driving forces on the non-agricultural sector; likewise, stimulating the informal urban sector makes it possible at once to increase supply and to generate income, expanding the domestic market.

On the contrary, for others, the development of the intermediary sector can reconcile the goal of employment and production (cf. Steel, 1980). Next to the modern sector, major transitional or national units, with high productivity levels, which should be situated within the logic of international competition, an intermediary sector must be allowed to emerge, making it possible to meet essential needs, serving to absorb workers, and finding an increasing place in the niches left by the capitalist firms within the framework of the DIT. Assistance to the informal sector can be made possible either through action on demand (e.g.: public contracts; redistribution of income to groups consuming the goods and services provided by this sector), on supply (e.g.: granting credit, access to low-cost raw materials and equipment), and the environment (price, fiscal and urban policy). Thus, for Nihan, "as a priority, assistance must involve activities showing a certain enterprise spirit, having capital and able to demonstrate job-creating potential." On the other hand, access to credit must be limited because of the risk of overcapitalization. For Steel, assistance to the intermediary

sector must involve the demand side rather than access to capital.

Regardless of economic policy debates, intervention with regard to micro-enterprises is a delicate process. By definition, institutions and organizations have trouble understanding something that goes beyond regulation and institutionalization. Intervening to institutionalize and regulate by intensifying the internal dynamics involves a great deal of risk. Incentive policies and the establishment of interfaces between micro-enterprise agents and the modern sector (e.g.: joint and several guarantee for credit, group purchasing, etc.) are preferable.

#### II.4. - The effects of adjustment policies on micro-enterprises in Madagascar

Because of the highly fragmentary nature of statistics on employment and reaction times for the effects of adjustment policies on the structure and evolution of employment, it is very difficult to evaluate the exact impact of these policies. Some trends can be noted:

- In administrations, the rate of new agent recruitment, which was about 10% in the seventies, fell to 1% between 1980 and 1986 (annual rates). The result, taking departures into account, was an overall decrease in the workforce. For example, in the area of agriculture, the ministry was cut in half in 1982; the employee workforce was reduced by 3000; several Government organizations were eliminated, and more financially-streamlined management procedures were implemented, limiting the "overabundance" of personnel. Adjustment policies lead as a priority to the deflation of the administration and the para-public sector, the main regulators of jobs for persons having degrees during the seventies.

In modern sector enterprises, authorizations for dismissals related to the general climate of economic stagnation, led to the practice of technical unemployment or the acceleration of personnel dismissals. Thus, in the industrial sector, which accounts for about 1.4% of total jobs, employment volume increased 4% per year between 1968 and 1978. Since the beginning of the eighties, this sector discharged over 400 workers per year. The only exception involves the water and electricity industry, which doubled its work force in ten years. The reason for the limitation of dismissals, considering that, on the average, enterprises operate at 40% of their production capacity, is attributed to government controls on economic dismissals (1973 text); in practice, enterprises are increasing disciplinary dismissals, voluntary departure incentive measures or the recourse to temporary labor.

On the other hand, the least capital-intensive "informal" urban activities have expanded. Studies conducted by OIT/PECTA in 1984 and 1985 on Antananarivo, Antsirabe and Toamasina make it possible to quantify this evolution<sup>12</sup>. According to the December 1984 survey of Antananarivo concerning 4 activities (wood, metal construction, garage, repairs), jobs provided by these 4 industries represented 25% of the workforce for labor in the industrial sector for all of the Faritany of Antananarivo, and supports 16% of the population of the capital (600,000). Overall turnover represents 3% of GNP and 12% of the industrial value of the country. With respect to the 1978 survey, the annual growth rate in the work force would be 2.5%, but, in reality, it is certainly much higher because of the different bases used for calculation, underestimating the 1984 work force. The study shows that the crisis in the industrial sector has greatly accentuated the competitiveness of this sector, even though the latter is running up against the limited management capabilities of the "entrepreneurs" and waste occurring in the use of production inputs. The Antsirabe study, mainly involving wood, garages and metal construction, shows a very high degree of dynamism in the non-structured sector in a city with a strong industrial component. Employment growth rates between 1980 and 1985 vary from 18 and 23% per year, depending on the sector. On the other hand, the Toamasina study, involving wood, public works, garages, clothing, repairs and fishing, shows a more limited degree of dynamism.

Organized according to non-wage social relationships, operating outside of official regulation, using unpaid labor, small in scale, and adapting to fragmented demand, small urban commercial activities have constituted essential ways of life and survival, but involve an involutive process of declining productivity.

- Survival strategies and behavioral change<sup>13</sup>

Facing a high degree of regression in the standard of living, vulnerable groups have adopted survival strategies reflected by behavioral changes with respect to the family group, work or consumption.

With respect to the family, we note a high increase in family instability (temporary or permanent separation), disorganization of the family unit (e.g.: family meals), an increase in commercial work on the part of women or children at the expense of domestic work, a trend towards limited births.

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<sup>12</sup>Cf. Gozo (1985).

<sup>13</sup>Cf. UNICEF/MPJS (1987).

The search for minimum income leads to the multiplicity of small-scale activities, increasing the duration of work and promoting monetized income; it also is reflected by a heavy accentuation of migratory movements.

#### The accentuation of migratory movements

Two contradicting phenomena appear at the level of migratory flows; on the one hand, insecurity and the decrease in nutritional potential have unleashed rural emigration and accentuated the differences within rural communities, but, on the other hand, we note urban emigration phenomena related to the rice supply crisis in the cities. Whereas migrations have traditionally been principally inter-urban, limited rural emigration was occurring in stages, oriented especially towards small urban centers, we note a profound change in this pattern. The gross rural exodus rate of 12% in 1975 was estimated at 29% in 1985. Intra-rural, urban/rural and rural/urban migrations have increased.

Two survival strategies can be distinguished:

- Regressive survival strategies are characterized by the recourse to illegal or a-legal practices: criminal activities, prostitution, child abandonment, child labor and theft in the urban environment; brush fires, standing crop or livestock theft in rural areas.

- Tolerable adaptation strategies are characterized by the search for complementary resources, compressed consumption, drawdown on savings or assets (land, livestock). Complementary resources result from the "informal" sector, indebtedness, multiple jobs, labor on the part of family members, and migratory phenomena. Consumption is adjusted in superfluous areas, as well as that of food; households increase in size; marriages are delayed and trends toward alienation in the family unit are observed. The accentuation of social differentiation in urban and rural environments leads to an accentuation of proletarianization and the concentration of assets (especially at the level of land and livestock).

#### Conclusion

The case of Madagascar can appear as extreme and caricatural, but it has the interest of enhancing the traits and highlighting certain factors. The numerous studies devoted to the effects of adjustment policies show that, if, on the whole, there has been a reduction in the foreign and domestic financial imbalances, this re-establishment of equilibrium has for the most part been achieved at the price of growth, placing the burden on the future (drop in investment) and in the great majority of the cases aggravating the poverty threshold (cf. Hugon, 1986).

In this context, the micro-enterprise sector has been a catalyst and a regulator for crisis; it has demonstrated great capacities for ingenuity and adaptation; in many cases, it constitutes a prerequisite for the efficiency of the major units. Considering its productivity, it is not obvious that it can appear, on the contrary, as an alternative model to major organizations and the establishment of an industrial system.

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