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**Partnership for Productivity**  
International

**A SMALL ENTERPRISE DEVELOPMENT PROGRAM FOR ECUADOR:**

**ECONOMIC BACKGROUND PAPER**

under the

**SMALL BUSINESS CAPACITY DEVELOPMENT PROJECT**

**(Contract No. DAN-5317-C-00-3085-00) for USAID Ecuador**

Prepared by:  
**Partnership for Productivity/International**

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Prepared for:  
**Private Sector Office  
U.S. AID Mission, Quito,  
Ecuador**

**JUNE 1985**



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## I.- THE IMPORTANCE OF THE SMALL ENTERPRISE IN THE DEVELOPMENT OF ECUADOR

### 1.- The Potential Contribution of Small Enterprise in Economic Development .

Small enterprise (defined broadly to include very small enterprises such as the artisan sector in Ecuador, but also larger establishments such as those referred to as Ecuadorean small industry) plays a different role in economies at different levels of development. It tends to be more important in economies at early and middle stages of growth. The main reason is that it has the capacity to produce using relatively large amounts of labor with modest amounts of the still scarce resources -- capital, imports, and sophisticated organizational capacity. Larger scale enterprises, for a variety of reasons tend to be heavy users of these scarce resources, while requiring little of the abundant resource, labor. As a result they tend to be, with as always some exceptions, economically inefficient in the early stages of development. The inefficiency is often disguised by high rates of protection against imports, by high levels of subsidy from the public sector, and so on. Awareness of this inefficiency is often blunted by the confusion between engineering efficiency (modern technology, high ratio of output to material inputs, etc, ) and economic efficiency; there is no necessary correlation whatsoever between these two. A further source of confusion is the tendency to equate efficiency with high labor productivity, when in fact high capital productivity is much more to the point. Finally there is a tendency to overplay the fact that large enterprise can create well paid jobs (especially when favoured by high levels of protection), but to forget how few jobs it creates; small enterprise jobs are not as clean, relaxing or remunerative, but there can be a lot more of them.

A good rule of thumb then is that in quite poor countries very small establishments are likely to be the most efficient. In middle income countries, an in-between size

category is likely to be most efficient, while only in developed industrial economies are many large firms likely to be on top of the efficiency spectrum, though even then small enterprise continues to play an important role due to its advantages of innovative capacity and flexibility. A quick look at which Ecuadorean manufacturing products are price competitive suggests that the main examples come from artisanry and small industry -- furniture, shoes, various items of textiles & clothing, etc.

With the rise in Ecuador's income, especially over the 1970s, the potential to compete (without any or much protection) should have gradually shifted from artisanry towards small and medium enterprise, and indeed the growth of these sectors was quite rapid over the decade or so prior to 1980. Large enterprise also did well, though at least in the case of manufacturing this probably owed much more to high levels of protection cum subsidy than to basic economic competitiveness.

The powerful economic logic which underlies the importance and economic efficiency of small enterprise in developing countries is corroborated by the important role played by this sector in many of the most outstanding success stories of development. In fact, to achieve both fast growth on the one side and high employment creation and poverty eradication on the other, a flourishing small scale sector is a very key ingredient, perhaps even a necessary condition. This is well illustrated by the case of Taiwan, where in both rural and urban sectors small industry and small enterprise in general has flourished over the last two decades and more. Not only has Taiwan's growth rate been one of the fastest in the world, but employment creation has been rapid, unemployment low, and income distribution more and more equal with the passage of time. All socio-economic groups have been major beneficiaries during this process, but the poorest have seen a truly astonishing growth in their income and welfare. When a country achieves rapid

overall growth without a large and dynamic small enterprise sector, as has Brazil <1>, the fruits of growth are usually highly concentrated, with the problems of poverty, underemployment remaining as sources of social strife.

A closer look at small enterprise reveals other advantages besides its ability to adapt to a country's abundance of labour and scarcity of capital. In most countries small enterprise is mainly self financed; in offering a productive outlet for the savings of the entrepreneur (and often his/her family and friends as well), it contributes to raising the country's rate of savings. Alternative outlets are often unattractive (cash and financial assets tend to offer low or negative real rates of return) or socially unproductive (e.g. investment in real estate). And, although small enterprise's contribution to technological advance may at first glance appear less striking than that of larger firms, it has in many countries been shown to be considerable. Further, the improvements which emerge from experimentation and the urge to do things better in small enterprise tend to be socially productive improvements; they contribute "appropriate technology" rather than the excessively modern and expensive technologies more likely to be the outcome of comparable efforts by large establishments.

Small enterprises are, by their very smallness, more likely to be part of a competitive sector than are large firms; this is especially so in a small country like Ecuador where one fairly large firm can, if well protected from the outside, easily become a monopoly. One of the important contributions of the smaller firms is to weaken monopolistic positions, to provide inducement to greater efficiency on the part of larger firms and in perhaps the most positive outcome of all, observed in Colombia's agricultural machinery industry in the 1970s, push the larger firms into the export market. Small enterprise not only competes with larger firms; it

also collaborates productively with them through subcontracting arrangements, and contributes to the efficiency of large enterprise by providing a training ground for workers, who then move to large firms, attracted by the usually higher wages available there. Very important also, some small firms grow into large ones. Put another way, most large firms started small. An efficient and dynamic small scale sector thus not only yields current benefits to a developing economy, but also provides the base for the larger establishments of the future, establishments which will some day be more competitive than they could now be since capital will then be more abundant.

A final point, of special relevance to Ecuador at this time, involves the role of government in the economy and in employment creation. It has been commonly observed that countries in the midst of mineral bonanzas, such as Ecuador in the 1970s, become service-oriented economies as far as employment is concerned, with the government sector playing a large role in employment creation. This is a result of the facts (a) that the mining sector itself usually creates an insignificant number of jobs; (b) money is relatively easily available to create public sector jobs and people clamour to get them; and (c) other productive sectors are put at a disadvantage both by the country's ready access to imports and its lack of attention to their development. Where the private sector does not provide reasonable employment options, people will naturally pressure the government to create jobs. The large scale sector has only a limited potential to create jobs because of its capital intensity. A prosperous small scale sector may be the only safety valve to relieve the pressure towards an overstuffed public sector. When it is not there to perform this function, one may see the extremes observed in countries like Malaysia, where relatively educated youth often remained unemployed for one to two years before getting their first job; their range of vision is the public and modern (large scale) private sectors, because the small scale sector is not of adequate

size to provide an alternative. For most the large scale private sector is out of reach, so the government will be faced with either creating unneeded or low payoff public sector jobs, or relegating people to the unemployment pool. An overstaffed public sector implies a number of problems above and beyond the excessive cost that it implies. For those so inclined, it provides a setting conducive to bad working habits. For those anxious to do something, it may be a temptation towards the taking on of responsibilities which might better be performed in the private sector, or which may even hamper that sector's effective functioning.

## 2.- Small Enterprise in Ecuador. History, Characteristics and Past Performance

The role and potential contribution of small enterprise in Ecuador's economy over the coming years must be understood in the light of the recent history of the economy, and in particular of the petroleum-based boom of the 1970s and the recession of the 1980s. The boom brought rapid income growth and structural change to the Ecuadorean economy; both output and employment growth were particularly fast in the public sector, in construction and in certain services. While by no means equally distributed, the fruits of the boom do appear to have been rather widely shared.

The boom did, however, leave the country with an income level out of line both with its level of productive capacity in the non oil sectors and with the administrative capacity of the public sector. As a result, in the absence of "easy rents" provided by petroleum it will now be hard for the country to achieve a fast rate of growth and even harder to attain a satisfactory pace of employment creation such as to prevent worsening poverty and accentuating inequality. Disequilibrium in the labor market is likely to become worse as a reduction of growth on the demand side coincides with a probably increasing rate of growth of the labor force; that growth

was somewhat curtailed in the 1970s by the rapid increase in educational attainment and by a still low rate of female labor force participation. These labor market trends are discussed in some detail in Annex B.

Whereas, the 1970s were a decade of widespread advance in Ecuador—in output, in incomes, in urbanization, in levels of education, and no doubt in levels of expectations and aspirations, the early 1980s have witnessed a slowdown of G.D.P. growth and in 1983 an actual decline. The growth pattern of the 1970s can clearly not be repeated in the rest of the 1980s, unless foreign exchange availability dramatically improves again, which is unlikely. The probable new scenario creates the challenge of shifting to a quite different pattern of growth. If the challenge is not successfully met, Ecuador's labor market is likely to be the scene of much turmoil, unsatisfied aspirations, and inefficiency in the coming years.

The economy of Ecuador has achieved a degree of recovery from its stagnation/decline of 1982-83. The output of factory manufacturing (including small industry and large industry but excluding artisanry) is believed to have grown significantly in 1984, <2> after the sharp decline in 1983, but according to recent Central Bank surveys, employment is believed to have continued falling in 1984, with a modest growth of 2-3 percent predicted for 1985. The Central Bank's sample, which covers firms with about two thirds of the productive capacity of the factory sector, includes mainly larger firms; if its prognosis is accurate, the large scale sector will make little contribution to employment growth in the near future. The construction sector, which is also in the midst of recovery, especially due to the public investment in the construction and repair of roads in the coastal area <3> should make a greater contribution. But the public sector presumably will not. This context places a greater than usual importance on Ecuador's achieving and supporting a dynamic small enterprise sector. The historical record suggests that this should be possible, as

long as the sector is provided with a reasonable context for growth and a modest level of support.

### 3.- The Size Composition of the Non-Agricultural Sector in Ecuador .

Most urban workers and, a fortiori, most non-agricultural workers are employed in small establishments. A recent study classified about 55 percent of the 1980 urban labor force as falling in the informal sector (Table A.1), with the major sectors, judged by the level of employment, being personal services, retail trade, and manufacturing. Major components of the formal sector are government (part of "other services"), manufacturing, construction, and part of commerce. It is apparent, if one considers the very fast growth of employment in the government and construction sectors over the 1970s, and the fast growth of the larger scale establishments in manufacturing, commerce, and to a lesser degree services, that overall the formal sector was indeed growing fast during the 10-15 years prior to 1980. Thus Ecuador's urban economy has been in transition from a quite "informal" system made up of small-scale production units employing rather traditional technologies, to one with a heavier weight of more formal or modern establishments. In sectors like manufacturing, modernity often goes with a larger scale of operations. Although over the 10-15 years prior to 1980 Ecuador's urban economy moved substantially towards the modernity end of the spectrum, having started from a low base in this regard, it is still a substantially informal system.

The most detailed data on the size structure of establishments come from the 1980 Economic Census , which covered most urban establishments in mining, manufacturing, commerce, restaurants and hotels, financial, business and personal services. (Transportation, construction and government were the major missing sectors.) As we can see in Table A.2, nearly two thirds of the persons employed in these sectors

(62.2 percent) worked on establishments of less than ten workers, while only 25 percent were employed in establishments of 50 workers or more. Were the data corrected for undercoverage at the lower end of the spectrum, these figures could move to perhaps 70 percent and 20 percent respectively. Excluding the mining sector, where petroleum production corresponds to a very large establishment, the output of the establishments of less than 10 workers in these sectors would be a little under 30 percent of the total, those of 10 to 19 workers about 9 percent and those of 50 workers and up about one half. Small enterprises are particularly important in commerce and in services. In the former case, the employment share of establishments of less than 10 workers was 80 percent in 1980 (See Table A.3), and the output share was close to 45 percent <4>. In manufacturing, although small establishments of under 10 workers dominate employment somewhat less than in sectors like commerce, they still account for a quite significant majority of total employment, about 60 percent of the total as of 1982. (For further details, see Annex C.).

Ecuador's well known tradition of artisan production of manufactured products, and of political attention to artisan manufacturing is in keeping with the importance of this subsector. Defined for the moment as including plants of less than 10 workers, it probably provided 80 percent of employment in manufacturing activities in 1962, falling to perhaps 70 percent in 1974 and then to about 60 percent in 1982 <5> (Table No.A-4). Such a decline in the relative role of smaller scale establishments is to be expected in the course of development, based on the experience of other developing countries. In the period 1974-1982, and in contrast to the period 1962-1974, growth of artisan and very small scale employment seems to have stagnated in absolute terms, while that in establishments of 10 or more workers grew by 60 percent.

As is evident from Table A-4, manufacturing employment during the boom period (or at least the latter part of it) rose fastest in the large scale sector -- plants of 50 workers or more. But growth of total employment in small industry (however defined) was also considerable. And the rate of growth of the typical small firm may well have exceeded that of large firms; part of that growth is unreflected in figures like those of Table A-4 since fast growing small firms move out of that category (whereas employment in the large-size category is swelled by firms moving into it from lower size categories.)

Small enterprise, as discussed earlier, tends to be more labor intensive than large enterprise; this is evident both for the economy as a whole and in each individual sector. For the sectors covered by the 1980 Censos Económicos, for example, the amount of capital (fixed plus inventories) per worker ranged was over 30 times higher in establishments of above 10 workers than in those with less than 10 workers.

For manufacturing, it appears that small industry is about a quarter or a fifth as capital intensive as large industry, while artisanry is, in turn, about a third as capital intensive as small industry. Associated with these wide gaps in capital per worker was inevitably a marked (but less wide) gap in value added per worker and in wages. Average earnings of blue collar workers in small manufacturing establishments of less than 10 workers were, in 1980, about 50 percent as high as in large establishments of 50 workers and up (Table A-6). Although less than what this modern manufacturing sector could pay, wages in small industry (10-19 workers, say) were well above those in agriculture -- perhaps twice as high in 1980. Both the labor productivity and the wage gaps between small and large firms appear to have been narrowing over time. Between 1965 and 1980, for example, the ratio of wages

(for all workers together) in establishments of under 10 workers versus those of establishments of 100 or more workers rose from 27.6 percent to 35 percent.

The average real wage in these small plants rose about 60 percent over this period as compared with 34.4 percent for the largest plants. Labour productivity also rose substantially faster in the small plants percent.

Small industry tends to use less imported inputs than large industry; as of 1980 the ratio of imports to value added was about one third to one half as high in the former as in the latter. Smaller scale manufacturing, less capital- and import-intensive than its large scale, counterpart, is disproportionately located in secondary cities and smaller urban areas <6>. Whereas in Quito and Guayaquil over 70 percent of recorded manufacturing employment in 1980 was in establishments of 10 or more workers, in the intermediate cities of Ambato, Cuenca, Portoviejo, Manta and Machala (taken together), the corresponding figure was 50 percent and in the rest of the country 32 percent. The increasing weight of factory manufacturing in general and of the larger scale component of it have been associated with an increasing regional concentration of manufacturing. Between 1974 and 1982, the share of total manufacturing employment which was located in the provinces of Pichincha and Guayas rose from 46.4 to 55.4 percent; the share in the four provinces where Ecuador's next five cities are located dropped slightly from 24.8 to 24.2 percent, and the share in the other provinces fell sharply from 28.8 percent to 20.3 percent as their absolute level of manufacturing employment also fell from 65.3 thousand to 57.9 thousand. Essentially all the employment increase of 58.6 thousand occurred in urban areas, an increase of 26 percent over the 1974 base. The urban employment increase was fastest in Pichincha and Guayas (51.7 percent), next in the four cited provinces (41 percent), and slowest but still positive elsewhere (17 percent). Rural manufacturing employment expanded nearly as fast as urban employment in Pichincha/Guayas (46.3 percent), rose marginally in the four provinces (8.4 percent)

and fell sharply (by 25.5 percent) elsewhere. In short, the performance of manufacturing employment was associated rather closely with proximity to the medium and larger urban centers. Rural manufacturing, which is typically quite small in scale, seems mainly to have flourished in the shadow of two metropolitan areas (rural Pichincha and Guayas) and in Tungurahua and Cotopaxi.

Small scale manufacturing is concentrated mainly in textiles/clothing, in wooden products (especially furniture), in food products, and in metal products. (Table A-5). With the partial exception of the last category, these are basic products which enter heavily into the budget of poorer families.

The characteristics of labor intensity, limited use of imports, production of basic necessities and greater regional dispersion than is true of large industry argue strongly for a continuing and expanded role for small manufacturing and small enterprise in general. So does the currently more stringent setting with respect to the availability of capital and foreign exchange in Ecuador. Much of the achievement of small enterprise in the past has been attained with little or no assistance from the public sector, sometimes in the face of serious discrimination by that sector. To maximize the sector's contribution in the coming years, removal of impediments and some degree of positive support will be important.

## II.- THE ENTREPRENEUR AND THE BUSINESS ENVIRONMENT

### 1.- Introduction

Entrepreneurship is the ability to combine and organize a number of physical and human factors to achieve a predetermined goal. This organizational skill can be applied to many forms of social behaviour, among them the economic or business activity, which is the central focus of this study. In this respect, the business entrepreneur must search for and find combinations of labor and capital that yield an output wanted by some members of the society. The business person faces two main challenges. One is to identify which among many possible combinations of labor and capital are the most efficient in an economic sense. The other is to find a market for that output. Both processes are simultaneous and each involves a great deal of uncertainty in the decisions to be made. The more knowledge, experience and information the entrepreneur has about production processes and markets, the less risky his decisions will be. The entrepreneur's main concern lies in whether he will be able to generate revenues above the costs involved in the operation. He knows that after he commits resources (his own or borrowed) to the operation, there is no guarantee that costs will be below revenues. Even if he identifies the possibility of making a sizable profit, the chances of failing may be too high and the cost of failure may be unbearable, to the point of inhibiting him from going into business.

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Uncertainty arises from many different sources. Some of them are intrinsic to the business operation and the entrepreneur himself; others depend on the general economic and political environment that surrounds and influences the business operation. To the first group belong the questions of whether the hired labor will perform properly, whether the machinery or equipment will work as expected and

whether the entrepreneur himself will be able to cope with all the problems that will certainly arise. The business environment adds to the general level of uncertainty through sudden changes in the domestic or international economy, unanticipated government policies affecting taxes, wages or interest rates, labor conflicts, etc.

Each individual entrepreneur has different perceptions of uncertainty and also different capacities to absorb risk. Those differences result from the fact that each entrepreneur has given levels of knowledge, experience, capital and even personal contacts that can help in obtaining relevant information to reduce risk. At the same time, entrepreneurs do not have the same perception of risk across economic activities or sectors. Some may find a particular sector relatively safe, while for others the opposite may be true. Though the perceptions may vary across sectors, a generalized perception of risk affecting agricultural or industrial activities, for instance, could influence entrepreneurial choice toward more passive forms of businesses, such as commerce or, if the entrepreneur has enough capital of his own, investment in real estate or outside the country.

## 2.- The Trade-off between the Entrepreneur and his Environment .

Economic development is not simply a macroeconomic phenomenon; it must take place at the micro level of individual enterprises. The entrepreneur is the one in charge of identifying the development opportunities at that level and combining the necessary resources to take advantage of those opportunities. Nevertheless, his ability to develop new opportunities is limited by the economic environment. The more constraining the environment, the fewer the number of entrepreneurs that will be able to develop new opportunities, or the more skillful, resourceful and financially strong the entrepreneurs will have to be to overcome those environmental

difficulties which are not simply due to the general perception of uncertainty. Historically, the existence of a very constraining business environment is accompanied by the existence of a small entrepreneurial class, that tends to be oligarchic and that can contribute to the general stagnation of the society. In order to break this vicious circle it is necessary to intervene in two directions. One is to create a business environment consistent with the development of established enterprises and the promotion of new ones. The other is to promote the growth of entrepreneurial skills and widen the participation of more individuals in the search for and exploitation of economic opportunities. The first form of intervention without the second will limit the benefits of development to the more privileged segment of the population. The second intervention without the first will also produce disappointing results.

A common group of environmental constraints result from a misguided conception of the functions of government that is generally reflected in inadequate legislation, excessive or ineffective intervention in factor and output markets and poor administration of government affairs. All this is usually accompanied by a poor human resource base that limits the number of productive or even employable individuals, and increases the chances that many people will be left out of the economic process. Under these circumstances a pervasive notion that opportunities are limited arises and a continuous and frequently violent struggle for survival sets in, leading to the belief that one person's gain is another's loss. In this atmosphere of distrust, the possibilities of finding mutually beneficial arrangements become narrow, and contractual relationships, an indispensable ingredient of economic and social development, become difficult and unstable.

### 3.- The Small Entrepreneur in Ecuador .

As discussed in chapter I there is a wide spectrum of enterprises in Ecuador in terms of size, representing a large variety of entrepreneurial skills. The majority of these enterprises, most of them artisans, live a precarious existence characterized by low labor productivity, limited administrative and technical skills, low levels of capital and limited possibilities for growth under the current circumstances. As reflected in the results of the survey of small industries specially carried out for this study <1> and of many other less formalized but more exhaustive interviews, there are many ways to improve the setting and performance of the small business sector in Ecuador. To the question "Which three services or forms of assistance would you like to receive to improve your business?", the three most frequently responded were: capital, technical assistance and training, in that order of importance. The answer on training covered skill development for the workers as well as for entrepreneurs themselves. In a separate question, "What will allow you to sell more?", 140 out of 200 answered "a better economic situation", while the second most important factor was "more availability of credit".

These results suggest that many entrepreneurs feel that the most important factor in the performance of their business is the economy -a stimulating expression of self-reliance- but believe that if they had more capital and knowledge, they could take better advantage of improving economic conditions. The importance attached to training and technical assistance clearly reflects an awareness of the profile of entrepreneurship discussed in the previous sections. That awareness extends to individual attributes, such as knowledge, and to environmental factors such as economic conditions and level of training of the labor force.

The shortage of capital results from both individual and environmental or macroeconomic conditions. The entrepreneur's ability to obtain credit depends not

only on his credit history or capacity to provide guarantees, but also on his knowledge and familiarity with credit institutions. The general availability of credit and the cost of obtaining it are determined by money market conditions. These conditions reflect the propensity to save in Ecuador, the net inflow of foreign funds, and the government's fiscal and monetary policies. The government's influence on the business atmosphere extends to the provision of public goods and services that could be particularly important to the small entrepreneur. Even though the private sector can play an important role in skill development through on-the-job training programs and other training formats, government institutions bear the main burden, especially in the case of Ecuador where the educational base is still weak.

The surveyed entrepreneurs show awareness of the importance of government institutions in general. However, many are ignorant of the existence of some valuable services. For example, only about half of the small manufacturing survey's respondents knew of the Ministry of Commerce and Industry (MICEI), 36 percent about the Council of Small Industry and Artisans (CENAPIA) and 40 percent about the Fund for Small Industry and Artisans (FOPINAR). This result may reflect variations in the ability of entrepreneurs to know about and take advantage of opportunities, or a need for greater promotion of public sector services. Since the resources available to foster small business development are limited, a possible policy implication of the inequalities in management skills (and perhaps motivation or drive) is that resources must be dedicated to the ones that seem to be most capable of using them. For instance, the enhancement of credit accessibility could be implemented by identifying those entrepreneurs more willing to undertake basic practical training and perform satisfactorily. This would serve to filter out the worst credit risks while improving the efficiency of financial investments in the small business sector.

Improvements in capital availability, training and technical assistance will reduce the uncertainty under which business decisions are made, helping consequently in the growth of the sector. As an increasing number of entrepreneurs become more sophisticated in the management of their businesses, other current limitations of the economic environment will become apparent to them. One of the most important is the lack of information regarding general business conditions and potential opportunities in Ecuador, which contributes to the risk of the business decisions. There are glaring gaps in statistical information that could be very valuable for economic decisions, at the level of government and also at the level of the private sector. One example is the non-existence of labor statistics about levels and variations of employment and wages. Another is the lack of data about business creation, growth or failure and their causes. In some cases, information exists but takes too long to be processed and made available to the public; this is true of household and industrial surveys, important tools for market research. Additional constraining variables regarding labor and financial markets will be discussed in the next two chapters.

It is important that policy oriented to entrepreneurial development, not be limited to the already established entrepreneur. There are no doubt many men and women who have not yet entertained the idea of going into business on their own or in association with others, but who could become prosperous entrepreneurs and make significant contributions to the national economy. Entrepreneurs do not constitute a closed group or class, even though, under the present conditions in Ecuador, entry by new entrepreneurs is more difficult than it should be. The identification and development of the virtually infinite number of goods, services and production processes that represent the highly specific components of economic activity, require the creative energies of many individuals. A reduced number of

entrepreneurs can only handle a reduced number of possibilities of economic development at every level. If the quantity and quality of entrepreneurs is low, many development possibilities will be lost. As these variables are hard to measure, their importance in economic development is usually overlooked. There is a widespread illusion in Ecuador that the government and state enterprises can adequately identify and develop many economic activities; though this may be true of some activities, increasing evidence points in a different direction--the small scale private entrepreneur. It is important to energetically promote the idea that anybody willing to commit the necessary sacrifices can, regardless of his or her socioeconomic origin, become an independent entrepreneur. The promotion of the idea, should be accompanied by an appropriate set of policies aimed at identifying those would-be entrepreneurs with maximum potential and giving them appropriate support for their independent and self-sufficient development. A mechanism to publicize successes and failures (perhaps newspapers or business magazines) could contribute significantly. Some details in implementing policy options in this regard will be offered in the final chapter of this paper.

### III. THE LABOR FACTOR

#### 1.- Introduction

The law of supply and demand rules in the labor market as definitely as in any other market. The lower the price of labor (in terms of wages and salaries), the more the entrepreneur will be willing to "buy", and viceversa. An employer hires a worker only if he expects that the additional revenues that the worker will produce are greater or at least equal to the total costs involved in hiring. If wages are very high, the additional revenues produced by an extra worker will have to be higher to economically justify his being hired. Thus, all things being equal, the level of employment that an enterprise can generate depends on the level of wages that must be paid.

The productivity of an enterprise, measured by its ability to generate revenues per unit of inputs of capital and labor, depends on its technological and managerial efficiency. Firms with higher productivity can afford to hire more workers at a given wage rate. At the same time, a worker who as a result of his skills and dedication is quite productive, will more likely to be hired than a less productive one. An efficient enterprise that also has well-trained and dedicated workers is prepared to generate more employment and pay better salaries, if the market can absorb all it produces. If the firm is unwilling to pay appropriate salaries it runs the risk of loosing its better workers to other firms.

Some enterprises are more sensitive than others to the price of labor, in terms of their willingness or ability to change their level of employment. For instance, a firm that, due to technological and administrative characteristics, can easily substitute capital for labor, will hire less labor and rely on more capital if the

level of wages increases relative to the cost of capital. Other firms with less capacity to replace labor with capital when faced with increases in the cost of labor will either pay the wage, or go out of business. A monopolistic enterprise is usually able to absorb higher labor costs, but if it can replace labor with more capital, it will definitely do the latter. On the other hand, a firm with many competitors and with narrow possibilities of substituting capital for labor, will only absorb higher labor costs if it is highly efficient, otherwise it may have to increase price or close up. Its disappearance will mean the elimination of a given number of jobs.

Minimum wages often have the effect of increasing the wage rate above a free market equilibrium rate. When firms and workers are very productive and the possibilities of substitution between labor and capital are narrow, the effect of a minimum wage could be negligible, and it may increase the total income that goes to workers as a group. However, if firms are not sufficiently productive or can easily substitute capital for the labor, minimum wages can generate a significant amount of unemployment and even decrease the total income going to the workers. Only the workers that keep their jobs will be better off, but possibly only in the short run. As total output and income is less than it could be under different circumstances the aggregate demand for goods and services will be reduced, shrinking the size of the market and affecting the levels of production of most of the enterprises in the economy. The increase in costs of production resulting from a high minimum wage may also be reflected in higher prices facing the worker when he spends his earnings. In this very frequent scenario, the benefits of artificially pushing wages upward vanish, but the illusion of gains to the worker persists due to the complexity of the causal relations involved. The political pressure from those who believe they are gaining coupled with the ignorance of those who are losing create a system of social irrationality that is very hard to change towards a more consistent

arrangement which takes due account of and appropriately reflects economic development possibilities.

A common oversimplification in applied economic analysis is to equate the price of a unit of labor services with the wage rate plus fringe benefits and any other costs such as hiring and training expenditures. When a worker is hired by an employer, however, there is a considerable amount of uncertainty on both sides as to how the contractual relation will work. There is no guarantee that the enterprise will recover the agreed upon costs of labor, since the actual efficiency or productivity of the worker and its consistency over time remains to be seen. The worker himself will also have certain expectations about the job. If those expectations are disappointed, his level of performance may suffer. This uncertainty prevents the employer from knowing exactly how much he will have to pay for one unit of "effective" labor. The unpredictable problems that may ensue add to the cost of labor, in terms of the opportunity costs associated with possible revenue losses. If labor laws make it very difficult or costly to fire a worker who does not perform well, the employer's perception of future costs of labor are even higher. This will deter job creation in the same way that an extremely high wage would have.

In a climate of unstable or hostile labor relations, the perceived or expected cost of labor is even higher. The threat of strikes or continuous conflicts add significantly to the cost of labor in terms of expected revenue losses. If in addition to labor instability, minimum wages are too far above market equilibrium levels, employers will try to move to more capital-intensive technologies, hire at wages below the minimum level (a generally illegal practice) or both. This is a sad paradox in countries with high levels of unemployment or underemployment, where the scenario described above is not uncommon.

## 2.- The Small Entrepreneur and the Ecuadorean Labor Market

The almost total absence of organized labor statistics in Ecuador,- with the exception of census data- constitute a major obstacle to analyzing the economics of employment and wages. In this section we use evidence from a variety of sources to describe the current situation and, as best we can, to see how it affects the small business sector.

Current perceptions-they cannot be called estimates- about open unemployment rates vary mainly between 7 and 10 percent of the labor force in Ecuador. There is always some embarrassment on the part of government officials for this lack of solid figures. Something similar happens with respect to underemployment which may be placed as high as 30 and 60 percent of the labor force, but whose level is no doubt highly dependent on the precise definition. Such figures illustrate the ambiguity that exists on this matter. The population census of 1982 produced an estimate of open unemployment for urban areas of almost 7 percent, while urban samples for 1968 and 1975 estimated underemployment (very broadly defined) at 30 and 24 percent respectively (Berry, 1984). It can be expected that both phenomena increased after the boom period ceased in 1982. Meanwhile our own estimates suggest that around 57 percent of the total labor force in 1975 and 54 percent in 1982 had earnings below the applicable minimum wage levels (See Annex E). Census data for 1982 show that almost 36 percent of the labor force are independent workers, 27 and 45 percent in urban and rural areas respectively (Berry 1984, Table No. 7). A plausible assumption is that a large majority of this group -with the exception of independent professionals, who are about 5 percent--earn less than the minimum wage. Since more than 50 percent of all workers earn less than the minimum wage a significant number, perhaps around 25-35 percent of the total labor force, belong to the category of paid workers. Assuming perfect compliance with labor and minimum wage laws by the

public sector, those "underpaid" workers are employed in the private sector. An important implication arises: as much as 70 percent or more of private sector paid workers may receive less than the legal minimum wages. Notice that underpayment is not equivalent to underemployment, since in many cases the worker's level of skill does not permit him to attain a productivity which would produce revenue equal to the minimum wage. The figure just cited includes agricultural workers, most of whom are known to earn below minimum wage levels.

Obviously, an important segment of the Ecuadorean labor force has no choice but to work at wages below the legal minimum. This situation is the result of several factors: a) low levels of productivity of enterprises, b) low levels of skills and productivity of some of the workers, c) insufficient investments in physical capital by the business sector and d) preferences by businesses to use capital-intensive techniques. A second result of these problems is the high level of unemployment and underemployment. The available evidence strongly suggests that, with all of these factors at work a simple policy of attempted enforcement of the labor laws will only worsen the employment scene in Ecuador and contribute to a reduction in the level of economic activity. More enterprises might be forced to pay minimum wages to the workers they hire, but they could not be forced to hire more than they can afford, and employment could fall sharply.

Our survey of small industries shows that employers have a clear reluctance to hire workers when sales improve. More than 46 percent of the 200 entrepreneurs interviewed in Quito and Guayaquil would prefer not to expand the number of permanent jobs if their sales grow. They would rather choose to create temporary jobs, increase overtime or subcontract. Of those expressing their intention not hire more permanent or temporary workers, 47 percent mentioned the high level of minimum wages as the main reason, 21 percent pointed towards the low quality of the

labor force and 17 percent wanted to prevent the creation of a labor union (Comité de Empresa)<1> which, according to the labor code, the workers have the right to organize when their number reaches fifteen in any establishment.

Though it is widely reported that small businesses subcontract significant amounts of labor to circumvent the labor laws, our survey did not produce consistent results on this point. In only 18 percent of the surveyed firms did subcontracting account for more than 20 percent of sales. Presumably this phenomenon was underreported since subcontracting can be viewed as signalling an illegal practice. Nevertheless, the respondents did not worry about declaring that their firms had no "Comité de Empresa"; only seven enterprises, out of 33 having fifteen workers or more in our sample, had a "Comité de Empresa". It is not illegal not to have a "Comité de Empresa" since the initiative to organize it lies with the workers themselves. Whether the low number of "Comités de Empresa" reported is a result of apathy from the workers or pressures from the firm was not established in our survey.

The importance of the small business sector in the creation of employment in Ecuador must not be underestimated, as noted in Chapter I. Also important is the fact that levels of productivity in this sector are not high, so that even though it can create much employment, many firms cannot pay the artificially high wages imposed by the labor laws. There is no argument about the fact that the equilibrium wages this sector can pay are undesirably low. However, it is also a fact that the Ecuadorean economy, at the present time, is not efficient enough to afford better wages for the poorest and least skilled segment of the working population. A realistic strategy to improve the standard of living of Ecuador must be based on increases in efficiency and productivity of the worker together with expansion of the labor generating capacity of the economy via the growth of the existing firms and the creation of new ones.

### 3.- The Roots of the Problem and the Principles for an Action Plan

According to 1982 census figures, 54 percent of the population ten years of age and above had a maximum of primary school. The proportion having secondary education, including these with only one to three years, is 35 percent. Individuals with some or completed higher education represent the remaining 11 percent (Berry, 1984, Table No. 13). Though these figures represent an improvement in relation to the 1974 census, the high proportion of individuals with only primary education indicates an educational inadequacy which, together with serious quality problems in Ecuadorian education, contributes to low levels of productivity. The increase in labor productivity for the overall economy over this intercensal period has been estimated at 27 percent (Berry, 1978, Table No. 6). On the other hand, real minimum wages increased 87 percent (See Table A- 6), a major inconsistency with the evolution of productivity. The productivity index represents an average of actual productivity at the level of individual firms. Only those firms that experienced increases in productivity at a level comparable to the increases in the real minimum wage could be expected to hire more workers, unless they were being hiring at wages below the minimum. Obviously most firms did not fall into that group and thus suffered a reduction in their capacity to increase employment legally.

The practice of hiring workers at wages below the legal minimum is widespread, especially among the smaller firms. This has the effect of reducing the contraction on the level of employment that otherwise would take place. Thus, it is not possible to know how much unemployment or uncreated employment can be attributed to unrealistically high minimum wages; the effect may even be small. But one thing is certain: unrealistic minimum wage legislation forces businesses to operate on what is technically an illegal basis, together with the workers who accept the

market wages. This systematic and pervasive practice contributes to a tradition of illegality that surfaces in many other activities of the Ecuadorean society, such as compliance with the tax laws.

The latest version of the labor code of Ecuador (Registro Oficial, 1978) reflects a high level of aspirations for the worker. Those aspirations are legitimate in principle, but are unfortunately quite divorced from the economic possibilities of the nation at this point. In its first pages, the labor code reflects a strong bias against the private enterprise system. It was written under the illusion that workers rights can be achieved by simple legislation and enforcement of the resulting laws, without any apparent awareness that those legitimate goals depend on the economic conditions and capabilities of the country. It would be unfair and inaccurate to put major blame for the economic difficulties of Ecuador on the labor code or the unions. But it is an unhappy fact that a very small minority of the national labor force actually benefits from such legislation, and it would be hard if not impossible to demonstrate that its benefits are greater than the problems it creates for the generation of employment in Ecuador.

In spite of all this, and as a result of a great deal of misunderstanding, distrust and lack of factual knowledge, labor legislation remains one of the great taboos of the Ecuadorean polity and economy. Notwithstanding the serious political implications of confronting this issue, no serious effort to promote the economic development of the country can neglect it. The challenge is to find and implement a course of action that could improve the rules of the labor markets and the welfare of the workers, without creating a political storm. It is obvious that any strategy would have to be pursued and introduced over a substantial period of time, particularly because there is a profound lack of trust between organized labor and the rank and file on one side, and the business groups on the other. The government

has been playing a sort of neutral role, yielding to the different groups intermitently. A case in point is the fact that the latest version of the labor code was formulated in 1978, under a not exactly antibusiness administration.

Before outlining the general principles for an action plan, it is necessary to emphasize that interventions cannot be unidirectional if they are to have visible effects. As stated before, the labor problem is not the only one that limits the growth of economic activity in Ecuador. There are many other points of policy actions that must be dealt with appropriately, such as availability of credit, technical assistance and training of the labor force. They are discussed elsewhere in this paper. The suggestions that follow must be understood in this wider context.

The organized labor movement in Ecuador is a political power to be reckoned with, in spite of representing less than 20 percent of the labor force, perhaps much less. The labor confederations exercise a visible leadership in the labor affairs of the country, but their actions seem to be motivated more by political and ideological considerations than by factual knowledge of the reality and economic possibilities of Ecuador. The lack of statistical information on employment, wages, productivity and business conditions, accompanied by the resulting absence of research and studies on labor economics, is a fundamental obstacle to understanding. Labor unions and their members must be moved towards a more technical and less political vision of their possibilities. This movement should be accompanied by a similar shift by the business sector, to make it more responsive to the needs of the worker and to contribute to a reduction in the lack of mistrust that currently exists. Also needed is an effective push to improve the quality of the labor force and of the entrepreneurial groups; increases in the efficiency of workers would have a greater effect if accompanied by improvements in firms' efficiency. More specific

policy options will be spelled out in the final chapter of this paper.

#### IV THE FLOWS OF CREDIT

##### 1.- Introduction

The nature of financial needs and capabilities of a small business varies according to its stage of development. The most crucial moment is usually at the starting point, when the savings of the owner or group of owners may be the only available source. In economies where the propensity to save is very low or the levels of income are so reduced as to impede any significant accumulation of savings by individuals, the creation of new businesses is severely constrained. In any case the starting business needs funds for short- and long-term purposes. Both types of needs are highly complementary and necessary, in various proportions, for the development of a business operation. As the firm grows and reaches a certain degree of stability financial needs grow, but financial capability also rises and becomes more flexible. The firm may develop its internal sources or funds or it may have established a credit history sufficient to obtain funds from other sources.

In societies with large segments of individuals with no resources of their own, the inequality in financial capacity predetermines an increase in the inequality of economic opportunity, since those persons most in need of funds tend to be least capable of obtaining them. This consideration is important in the framework of the objectives of this project. Short run financial efficiency considerations lead institutions to prefer financial policies that are safer, by concentrating on the firms that are more efficient. The inefficiency of this mechanism will appear in the long run after the concentration of economic activity and opportunities in a few hands prevents many potentially successful entrepreneurs from making contributions to economic development. The high risk of lending to the poor entrepreneur cannot be born by the private lender. As the social and private benefits could only be

materialized in the long run, the short run risk will have to be absorbed as a whole by the society as a whole.

However, availability of funds alone is not sufficient to assure the generation of new businesses. Inability of an entrepreneur or his firm to invest and recover the investment with a profit can be an important bottleneck as well. As there are wide differences in the managerial abilities to invest across enterprises, perhaps the main problem in channeling credit to a wider segment of the small business sector is the identification of those who are most capable to use credit profitably. The point does not contradict the previous considerations about the advantages of reducing the inequalities of the distribution of credit. The possibilities of channelling credit to a substantial segment of the small business sector involve a certain amount of risk that can only be reduced by carefully selecting the credit subjects. The capacity of a firm to use credit profitably varies not only with the level of managerial skills but also with the size of the credit. Too large a loan could create more problems than it solves for a small firm with a modest level of organizational skills. The central message is that the development of small businesses by credit enhancement must go pari pasu with the promotion of other capabilities.

It can be argued that the most efficient way to handle the credit needs of the small business sector is to let interest rates reflect the level of risk carried by their borrowings. The effects of interest rate policy, either on the economy as a whole or on small business, are hard to pin down. Simple, though not necessarily completely misguided, models of economics, suggest that "below equilibrium" rates will (a) discourage savings and (b) lead to a misallocation of credit if a rationing system is used rather than the market. The cheaper the credit, the more likely, in this view, that it will be used for low pay-off projects, for real estate

speculation or for consumption. A low interest rate is also, of course likely to stimulate capital flight.

Additional complexities arise when there is a wide dispersion of interest rates, as seems to have become the case in Ecuador. Then there is an obvious incentive for any cheap credit to be channelled by the individual borrower to the high paying assets, as has recently been occurring with the introduction of "Polizas de Acumulacion" (issued by commercial banks) and "Certificados Financieros" (issued by financial corporations) with interest rates that float freely. Frequently, the lower interest rates are designed to favor firms assumed to be less able to pay than others, artisanry and small industry being examples. This can lead, depending on the way the system is structured, to a shortage of loans in those sectors, as well as to a "gathering of vultures" around the loans that are "soft", resulting in a squeezing out of those not well placed in the queue, for whatever reason. Thus, it has often been argued that small firms do better when the interest rates which they have to pay are high than when they are low. Unfortunately it is hard to quantify the various effects at work.

The arguments for low interest rates are different and associated with the idea that worthwhile projects may not be undertaken unless favoured with a relatively low rate, and that even if low rates create an excess demand for credit an adequate control/rationing mechanism can lead to an efficient channelling. Low rates for small enterprises have an additional problem in that the cost per sucre moved is higher, so the disincentive for the banks is correspondingly greater. Where low rates are combined with an administrative apparatus subject to bribery, these payoffs eat up part of the softness of the rate, while by no means necessarily inclining the system towards an efficient allocation of credit.

## 2.- The Patterns of Credit in Ecuador.

Credit statistics regarding the small business sector are limited to the small industry and artisanry (SIA) classified as such under the Law for the Development of Small Industry and Artisanry (MICEI, 1982). This law allows classified enterprises to obtain soft loans through the "rediscount" mechanism of "financial funds" held by the Central Bank of Ecuador. The borrower can apply to the National Development Bank (Banco Nacional de Fomento) or through commercial banks for those loans. These institutions can then "rediscount" up to 90 percent of the loans at the Central Bank. The loans carry a maximum interest rate of 18 percent according to a Monetary Board Resolution of December 11, 1984. There is an additional commission charge of up to 3 percent. Other small businesses, such as commercial establishments, are excluded from this special treatment. There are no organized statistics on the volume of credit that goes to small industry and artisanry outside this system.

Table A-7 shows the evolution of the total credit granted by the Ecuadorean banking and financial system to the small industry and artisanry sector coming under the above cited law, in relation to the credit going to other sectors.

In 1972 SIA's share of total credit was a meagre 1.24 percent; it started to grow in 1973 with the appearance of "Financial Funds", and peaked at 4.32 percent in 1976. Since then, that proportion falls until 1980, then remained about constant through 1982. Data are not yet available for 1983 and 1984. A similar trajectory is followed by SIA's share of the total credit going to the manufacturing sector. It began at 7.33 percent in 1972, increased to 19.84 percent in 1976 and then fell thereafter. During the same period the manufacturing sector's share of credit to the whole economy grew continuously with the sole exception of 1981.

As the figures are in current sucres they overestimate the real growth of credit.

Prices of manufacturing goods (as measured by the sector's implicit deflator) grew 2.26 times from 1975 through 1982, while credit to SIA increased by 4.3 times, indicating a 90 percent increase in real credit. Between 1979 and 1980 SIA credit decreased in real terms as the rate of growth of prices exceeded that of the credit. With the introduction of FOPINAR there was significant recovery between 1980 and 1982 as SIA credit grew by 68 percent and prices by only 17 percent. The effects of the dramatic devaluation of the sucre in 1982 cannot yet be ascertained.

In our survey, 23.4 percent of those receiving credit declared having received it through private (non-institutional) lenders. The figures show that 54.5 percent of the respondents declared having had access to either Banco de Fomento or commercial bank loans. Presumably most of those credits were negotiated through the rediscount window but its proportion cannot be established. These results are consistent with the fact that credit accessibility is the top priority for small businesses. A surprising and rather puzzling finding of the survey is that almost 60 percent of those who did not receive credit in the last two years have been in business for at least six years. nevertheless their ability to qualify or make good use of credit is not known.

### 3. Policy Implications

In developing countries, bottlenecks come in groups, but the most visible one hides the existence of others. Credit would appear to be the most important vehicle for accelerated development of the small business sector in Ecuador; certainly the entrepreneurs tend to cite it most frequently. But this perception may be rather misleading. Credit is often cited because the businessman is unaware of other problems. It may appear attractive partly because, as now, it is subsidized. In

any case, a rapid enhancement of credit availability may rapidly bring firms up against other limitations. The most important appears to be the level of administrative and technical skills of the small firm. Another, for some firms, is the perceived high cost of labor. For such firms, credit enhancement without parallel improvements of the utilization of labor, and/or reductions in its cost will produce a greater reliance on capital-intensive techniques, an outcome inconsistent with the promotion of "appropriate technologies" that could help create employment. Such entrepreneurs perceive labor-substituting machinery as cheaper and better behaved than labor. On the other hand, an artificial increase (e.g. via taxes) in the cost of capital goods will not necessarily stimulate more labor-intensive techniques, since the resulting increase in total costs may simply discourage production and thus reduce the possibilities of creating employment. Credit availability can be enhanced in the relatively short term while problems can probably related to labor inputs only be dealt with in the longer run.

Harsh reality indicates that there are no simple quick ways to reap the full potential of the small business sector, either in terms of its intrinsic capacity to grow or in terms of its employment creating potential. Thus, an effective policy package must include both short and long term interventions. As labor problems seem to affect primarily the largest of the small firms, it appears appropriate that credit enhancement be mainly focused on the smallest enterprises, generally the ones with less than fifteen workers, including the microenterprise. Improvements in managerial skills are important at all levels.

Regarding microenterprises, the experience of the highly promising experiments of FED, PRODEM and the "Grupos Solidarios" suggests that credit risk associated with the poorest entrepreneurs is not as high as often believed. At the same time the credit that individual beneficiaries in these groups could effectively absorb is a

limited. Probably the total credit flow required to satisfy their needs is modest. These considerations return the spotlight to the small enterprise below fifteen workers. Even if they prefer capital-intensive techniques, and their small size in spite of labor problems that cannot be solved in the short run, their small size tends to make them effective generators of employment. Therefore, in the short run it would appear wise to concentrate credit enhancement on the most efficient of that group of firms, while simultaneously increasing the credit access of the microenterprises.

## V. OTHER POLICY/PROGRAM AREAS

### 1.- International Trade

As noted earlier, Ecuador's international trade policy is in the process of significant change towards a more outward oriented regime. This is undoubtedly a generally wise shift of policy, since the country needs to generate new exports to replace oil and since the level of protection previously assigned to certain industries was probably excessive. It is to be hoped, both from the point of view of the economy as a whole and that of parts of the small scale sector, that the shift is not so brusque as to demolish some industries which in a reasonable period of time could become competitive, were they not facing distorted factor prices. We presume here that nothing approaching the extreme of the Chilean experience will occur, but that the new trade regime will be reasonably coherent and will not be introduced in an unduly jerky fashion. A good approach to tariff reduction, always bearing in mind the level of effective as well as of nominal tariffs, would be to phase the tariff cuts over a matter of several years to allow business a reasonable period of time to adjust.

The new trade regime should retain some reasonable anti-dumping safeguards, since for some products a small market like Ecuador's can be flooded readily.

Apart from the appropriate care being taken in the transitional period, a more outward oriented approach should not harm small industry, as long as reasonable assistance in the adjustment process is made available (including information on market opportunities, alternative products, etc.) and provided that factor market imperfections do not constitute too heavy a weight for the sector. Further improvements in credit access and steps to facilitate a smoother functioning of the

labor market (both discussed in previous sections) become more crucial as the protection against import is removed and careful combining of tariff and exchange rate policy is also important. As trade is liberalized and protection cut back, it becomes increasingly important that an overvalued currency not produce unduly low prices imports. A properly valued exchange rate also discourages capital flight and contraband.

One of the major booms to small manufacturing (and some other small scale activities) is a good market for second hand machinery. Such a market played a useful role in the dramatic expansion of small industry in Colombia during the 1970s. It especially aids the new investor with limited funds, since prices are often a quarter or a third those of the comparable new machine. It appears that this market is of limited scope in Ecuador, perhaps partly because the larger firms which in some countries sell their used machinery to smaller firms, here tend to use them until they have little further productive value; this may reflect the fact that modern machinery has not been seen as essential, given the absence of a need to compete in the domestic or international markets. Due to the lack of a domestic supply of used machinery, imports become important; absence of tariff and other barriers on these imports is particularly important, and a service to assist the information flow to the small producer particularly useful.

## 2.- Technology and Management

Partly because of its relatively recent development, Ecuadorean small manufacturing (as distinct from artisanry) has what might be called an unsettled situation with respect to technology and management. A number of errors in choice of machine technology have resulted from lack of information on alternatives, from lack of experience in dealing with machinery salesmen, and so on. Most branches of

artisanry, on the other hand, have a long history in the techniques they use. In all small scale sectors, though, there are usually many ways in which technology or management or both can be improved. Much evidence shows that small scale producers are often on the look-out for better ways to do things, and many show great ingenuity. Many public sector purveyors of technical assistance presume that the businessman is less capable than is really the case, while erring in the opposite direction in regard to their own capacity. Good advice on technological matters usually comes from someone who knows the specific case very well. On administrative, accounting, financial and sales matters many entrepreneurs are much less well prepared; this remains a major area where large benefits seem possible via relatively simple and general types of assistance, but even here a good deal of case specific attention is usually necessary for really good results.

While it is fairly widely recognized that the modern sector must in the long run get more and more productive technology if an economy is to develop satisfactorily, it is less generally known that the small-scale sector can make a larger and more substantial contribution to growth cum employment creation the more its technology is improved. The evidence from Colombia, where labor productivity in small manufacturing grew at a healthy 2 percent a year over a period of several decades, shows what can be done. In artisanry also many improvements are possible. In this sector it seems particularly necessary to move away from the attitude built into the Ley de Defensa del Artesano of 1953, which while protecting an artisan elite (those who qualify as titulados and are thus in a position to benefit from credit and absolution from worker benefits for which most other employers are at least technically responsible) provides neither mechanisms nor incentives whereby the sector could introduce new techniques and raise productivity. Yet scattered evidence makes it rather clear that the sector does have the potential to do this.

### 3 Fiscal Incentives

Most fiscal incentives are designed to stimulate modern, larger scale activities. And most also have the effect of encouraging the utilization of capital rather than that of labor.

Figures of Table A-8 show the tariff exonerations received by small industry and artisanry (presumably nearly all by small industry). The machinery import benefits from these exonerations presumably represented a high share of total such imports by small industry, and the "fiscal sacrifice" represented around 15 - 20 percent of the CIF value of the machinery in most years. But these exonerations were no doubt much more important for large scale industry (though no figures are available) since it is much more capital intensive and probably imports a higher share of its capital from abroad.

### 4 Access to Material Inputs and to Product Markets

The small enterprise is normally at a disadvantage in input markets because of its small size and lack of capacity to extend credit and/or to pay cash. The same may occur in the market where it sells, though this is a less frequently voiced complaint. Cost of input acquisition is usually higher in small firms than large, both in terms of the actual price and of the time cost involved. Since in many cases a number of small producers of a given item are located in close proximity to each other, it may often be possible to attack these problems through group purchasing, via co-operatives or some like institution. The same applies in some cases on the selling side. In small industry, as in small agriculture, there are often few economies of scale in the actual production process, but significant ones

in the related commercial activities.

##### 5. The Question of Quality Standards

Small industry sometimes produces low quality products and sometimes products of unequal quality. <1> Under some circumstances this may call for intervention (provided the intervention can be efficient), either to assist in quality improvement or to legally force it. Under other circumstances, a push toward quality maintenance would be counterproductive. Thus, any organization charged with ruling on quality issues needs to exercise careful judgement in determining when intervention is desirable. When low quality of a product is a result of limited use of resources, when the low quality is recognizable as such by the buyer, and when the product hence fetches a lower price, there is no reason for intervention to force an improvement in quality. If the buyers in question desired a higher quality and were able and willing to pay for it, they would usually already be doing so and suppliers would have responded to their needs. To force quality up could cut such (usually poor) buyers out of the market; it could also block the progress of small firms who get their start using simple technologies and unskilled workers, but who have the capacity to grow over time and indeed to raise quality. Interventions which can raise quality without raising costs are desirable but they do not require legal interventions but rather dissemination of information.

~~The need for quality control in order to enter foreign markets should mainly result~~  
from market pressure, from traders or the producers themselves. Qualified purveyors of information on how to raise quality are of course useful and may be an effective instrument. Where low quality presents dangers that the buyer cannot easily detect, there are grounds for intervention. But in general a public sector like Ecuador's would do best refraining from intervention except in quite clear cut

cases, both because efficient intervention is more easily conceptualized than carried out, and because businessmen tend to resent it.

#### 6. Minimization of Harrassment

Many regulations in Ecuador seem, de facto, to have the effects of (a) bothering or harrassing business, (b) creating unproductive employment in the public sector, and (c) creating situations which induce corruption. The government of Ecuador's concern about this problem is well founded, and the recent World Bank loan to study how unnecessary bureaucratization may be reduced is a fine initiative. Unnecessary bureaucracy creates certain costs for all types of business, but often these are greatest for the small businessperson who has less education and experience, can less afford the time involved in meeting bureaucratic requirements, and who may be less able to bear the cost of bribery to avoid a regulation which is without valid purpose.

A thorough thinking through of which regulations are really necessary and implementable is clearly a high priority matter for the government. Removing resources from those areas which do not fulfil these conditions would make it more possible to apply the really needed regulations with the vigour they deserve.

## VI. THE MACROECONOMIC POLICY-PROCESS AND THE SMALL-ENTERPRISE SECTOR IN ECUADOR

The connections between macroeconomic policies proper and the situation of the small-enterprise sector are indirect and mediated. These policies should, therefore, be distinguished from those that affect small enterprises directly. Thus, before discussing the extent and manner in which macroeconomic policies impinge on small-scale activities, their distinctive nature vis-a-vis sector-specific policies should be established.

### 1.- Macroeconomic Vis-a-Vis Sectoral Policy

Macroeconomic policy aims at simultaneously achieving "internal" and "external" balance in the overall economy. Internal macroeconomic balance is generally understood as the maintenance of as high a level of aggregate demand as is consistent with an "acceptable" rate of inflation. What is "acceptable" inflation varies, of course, with time, place and circumstance. External balance, on the other hand, refers to equilibrium in the balance of payments which, in countries like Ecuador, where nominal exchange rates are fixed or float in a managed fashion, boils down to having a "comfortable" level of foreign exchange reserves in the Central Bank. In practice, what is a "comfortable" level is gauged in Ecuador in terms of the number of months of imports that the Central Bank's foreign exchange reserves can cover at a given point in time.

Fiscal, monetary, and exchange-rate policies are the macroeconomic policies par excellence. In Ecuador, fiscal policy falls under the sphere of action of the Ministry of Finance <1>. Monetary and exchange-rate policies, on the other hand, fall within the domain of action of the Monetary Board and the Central Bank.

Sectoral policy in its most general scope emanates, in Ecuador, from the planning institution (CONADE) and the sector specific ministries. Policies particularly concerned with small-scale enterprises are a subset of general sectoral policies and, at least with regard to policies originated in public-sector institutions, are constrained and guided by the overall development plan adopted by the incumbent administration. The vast array of institutions, both public and private, that have a more or less direct preoccupation with the small-enterprise area is described at length in a separate background paper.

Speaking in broad terms, macroeconomic policy deals with short-term stabilization problems (such as inflation, balance of payments disequilibria, etc.). In contrast, sectoral policy is generally concerned with the performance of given sectors and the overall sectoral structure of the economy; as such, it tends to have more of a medium and long-run time horizon and is part of the government's development strategy usually crystalized in a multi-year development plan.

From the point of view of the small-enterprise subsector, the distinctions made above open three broad areas of policy-making processes that need to be examined. There are first, the nature of the possible linkages between macroeconomic policies and the possible performance of small enterprises; second, the relative importance given to small industries in the formation and implementation of the overall development plan, summarized in the "Lineamientos del Plan Nacional de Desarrollo"; and third, the characteristics and scope of policies specific to the small enterprise subsector operating within the constraints imposed upon them by stabilization (macroeconomic) programs, on the one hand, and the nation's development plan, on the other. The third area is examined in the institutional background paper referred to above. In this chapter, we comment briefly the first area.

## 2.- Interaction Between Macroeconomic and Sectoral Policies

There are at least three levels at which macroeconomic policy interacts and overlaps with sectoral aspects. The First is the level of the actors involved in the design of macroeconomic policy packages. The second concerns the selection of the policy instruments which are to be used to achieve a given macroeconomic target. The third refers to the level of the effects of macroeconomic policies on the relative performance of certain sectors or subsectors.

### 2.1. Participation in the Policy Process .

With respect to the first level, it is important to note that the small enterprise sector in Ecuador has no direct representation in the relevant bodies charged with the formulation of macroeconomic policy. Under situations of balance of payments crisis such as the one affecting Ecuador since the early 1980s, the two most important organizations in macroeconomic policy formation are the Monetary Board <2> and the IMF. They jointly negotiate the "stabilization package" which, once approved, opens the doors for IMF emergency loans and, as a consequence, for a potential normalization of foreign-debt negotiations with international private banks.

It is reasonable to assume that the fact that certain sectors and/or social classes are represented in the Monetary Board while others are not, has some influence on the particular characteristics of the stabilization programs and on the concrete combinations of policy instruments selected to achieve, say, balance of payments adjustment.

However, it is doubtful that narrow sectoral or class interests dominate over the general macroeconomic need for adjustment which, to a large extent, cuts across sectors or classes. Furthermore, the final outcomes of a stabilization program tend to be determined in the larger national political arena and not solely within the confines of the Monetary Board-IMF discussions. Thus, for example, while the fiscal and monetary restraint typically included in an IMF conditionality package often implies, at least in the short-run, a reduction in real incomes, how this reduction is to be distributed among different social groups depends on a wide range of variables; notable among these are the characteristics of the administration's constituency, the degree of democratic openness in the society, and the relative political strength of the various interest groups. In this respect, small entrepreneurs as a group lack the political visibility, the level of organization and the degree of institutionalization that characterize other groups in the Ecuadorean society, such as the chambers of commerce and large-scale industry or the unionized urban workers. In sum, neither in the sphere of the Monetary Board nor in the larger national political arena do small entrepreneurs have significant representation and influence.

It could be argued that the addition of a representative from the small scale productive sector to the Monetary Board is likely not to make a significant difference as far as the more typically macroeconomic policies are concerned. However such an addition, if accompanied by an improved organization and institutionalization of small entrepreneurs as a group, could have a noticeable effect with regard to other policies originated in the Monetary Board which are more sectoral in nature. Such is the case of tariff policy. Though tariff levels have macroeconomic dimensions (e.g. as revenue-raising instruments or as antinflationary instruments) they are and have been used in Ecuador as devices to protect or stimulate certain productive sectors over others. The small industrialist's

perception that the tariff system has important effects on their business has surfaced in informal interviews conducted throughout this research. Furthermore, the forthcoming publication of numerous reforms to the tariff law has heightened small industrialists' preoccupation with the topic and has underscored their lack of representation in the pertinent decision-making process.

## 2.2. Unintended Sectoral Effects of Macroeconomic Policy .

A significant share of the differential sectoral impacts of macroeconomic policy are not intended. Thus, the pursuit of a reduction in the government's budget deficit and of discipline in the credit-creation process that has generally characterized recent Ecuadorian stabilization programs, has aimed mainly at restoring overall economic equilibrium without a deliberate goal of affecting the relative performance of given sectors. True, all sectors have experienced a marked deceleration in their rates of growth in the midst of general slowdown of economic activity; however, the sectoral reaction to the changed macroeconomic environment has not been symmetrical. The results of our survey of small industries reveals a heterogeneity (at least in terms of employment) of reactions.

Asymetries in sectoral responses which are not a deliberate goal of macroeconomic policy are related to a variety of factors involving both the demand and the supply sides of the economy. The investment component of aggregate demand is generally very sensitive to changes in overall economic activity but tends to exhibit sectoral differences that ultimately depend upon the investors' perceptions regarding relative sectoral profitabilities in the future. The consumption component of aggregate demand, on the other hand, shows differential sectoral changes depending on the income elasticities of demand for the products of various sectors and on the possibilities of substitution in consumption. In this latter respect, one could

... hypothesize that since small enterprises tend to have a relatively large share in the production of wage-goods (food, clothing, etc.), the unintended effects of a contractionary macroeconomic policy on the demand side might be less severe for small enterprises than for larger ones, which tend to produce highly income-elastic "luxury" goods. Nevertheless, unintended sectoral effects of macroeconomic policy may be more serious for small enterprise than for larger firms. Consider the following three recent Ecuadorean illustrations; (a) a tight monetary policy expressed in a general contraction in credit availability; (b) a macroeconomic decision to abruptly raise the minimum wage; and (c) a major overhauling and liberalization of financial markets via interest-rate reform.

Under monetary policy small enterprises are likely to suffer disproportionately because of their more limited access both to imports and to those credit lines not specifically directed to the sector, and the relatively low "collateral" their being less important clients of banks, and the absence in their case of the sort of symbiosis often characterizing the relation between banks and large enterprises. In case (b), assuming that minimum-wage hikes have an effect on the overall level of wages, small industries producing wage goods might benefit as much or more than other firms from the resulting aggregate demand effect that could stem from the restoration of purchasing power in wage income. However, the demand effect is likely to be offset by the cost-side effects of a sudden increase in the minimum wage; in particular, an unintended greater burden on small enterprises may come from the fact that smaller firms tend to be more labor intensive than larger ones and hence to have a larger share of labor costs in total costs. Furthermore, if minimum wage adjustments are abrupt and irregular, as has been the case in Ecuador, they are likely to exacerbate the unemployment situation-not only because of the increased nominal cost of labor but also because of increased uncertainty-facing firms.

Finally, a recent Ecuadorean version of case (c) is given by the Monetary Board's Regulation No. 214-84 of December 1984, which introduced profound changes in the interest-rate system, raising the ceilings for all interest rates and allowing floating interest rates for two types of financial instruments, the Polizas de Acumulacion (Issued by Commercial Banks) and the "Certificados Financieros (issued by financial corporations). This was a macroeconomic policy whose ostensible goals were mainly to bring into the formal financial market a sizable volume of funds which was flowing through the "curb" market ( mercado extrabancario ) and to raise the aggregate level of domestic savings. However, given that a wide dispersion among interest rates has still been kept, unintended sectoral effects have begun to take place. In particular, for the small entrepreneur experiencing lower rates of return from his/her firm, an attractive possibility has been opened for shifting away from productive assets towards financial assets. Furthermore, a strong incentive for credit diversion is implied in this macro policy. In fact, it has become profitable for many an entrepreneur to borrow from, say, the Banco de Fomento at a (st.4) fixed nominal interest rate of 18 percent annually, and to put all or part of the borrowed funds in a "Poliza de Acumulacion" which is now paying a yearly interest rate of about 33 percent.

### 2.3 Sectoral Components Mixed With Macroeconomic Policy Instruments

Asymmetric sectoral reactions to macroeconomic policy are not only of the unintended type. Frequently, a macroeconomic policy package contains deliberate sectoral elements, i.e. certain provisions designed to execute macroeconomic policy within the guidelines given by the system of incentives embodied in the overall development strategy of the country. Quite often, this sort of situation arises when the instruments chosen to achieve a given macroeconomic target include deliberate sectoral differentiations. This can be better understood by choosing a concrete

example from Ecuador's monetary policy.

Since the monetary authority cannot control the level of foreign exchange reserves in a system of fixed official exchange rates such as Ecuador's, the money supply is usually controlled by managing the rate of expansion of domestic credit. Monetary policy in Ecuador is thus based on so-called financial programming, which after considering projections for inflation and GDP growth as well as estimates of future foreign exchange reserves, yields as a residual the rate of domestic credit expansion compatible with a desired growth in the money supply. A tight monetary policy thus means tight credit. However, there is a certain flexibility in the selection of instruments which are to be used to achieve the macroeconomic goals of financial programming. Constrained by the macroeconomic policy target, the choice of instruments is also limited as well as guided by the government's overall development strategy. Thus, if that strategy involves a conscious decision to promote industry and agriculture over commerce, as was the case of the Roldos-Hurtado administration, the desired reduction in the rate of the domestic credit growth is often accomplished via deliberate differential decreases in the credit available for those sectors. For example, credit ceilings are imposed on commercial banks' loans to commerce, while credit to agriculture and industry emanating from the Banco Nacional de Fomento or from the private banking system through Fondos financieros, are either exempted from the ceilings or subject to higher ceilings. Consequently, the level of available credit to small enterprises in a context of general illiquidity depends, to a large extent, on the relative importance given to those enterprises within the priorities of the nation's development plan, and on the degree of practical relevance that this plan has as a guideline for policy making. It is our impression that on both counts, the importance of the small-enterprise sector has suffered a relative decline in the Febres administration as compared to the Roldos-Hurtado government.

Further examples of the effects on small enterprise of deliberate sectoral components mixed with macroeconomic policy instruments can be found in other areas. We mention only a few: (a) the interest rate, a macroeconomic policy instrument, is often differentiated to reflect explicit credit preferences for some sectors or subsectors over others; (b) the minimum wage--again a macroeconomic policy tool--is in Ecuador not uniform; since 1980 a lower minimum wage rules for small-industry and artisanry than that applicable to large-scale industries; (c) the average tariff rate, itself a macro variable, is embedded in a highly differentiated tariff system reflecting, grosso modo, a preferential treatment for certain sectors and industries; and (d) the exchange rate is also differentiated, with a lower one applying to certain foreign transactions (such as the external debt payment) or certain imports deemed "essential", i.e., included in priority import "lists". It would be fruitful to explore the relative position of the small-enterprise sector in the choice of the sectoral components that are embedded in the macroeconomic policy instruments listed above.

### 3.- The Major Current Direction of Government Policy

The end of the oil bonanza and the balance of payments/debt problems and recession of the 1980s have contributed to the re-orientation of economic policy by the present Febres Cordero administration. One basic shift is from the heavy orientation towards import substitution, pursued in varying degrees during the 1970s to the present, to a more export oriented approach, with less protection for domestic industry. Tariff changes are to be announced soon. It is assumed, and policy steps consistent with this assumption are being taken, that the primary sector and especially agro-industry will become a major source of exports when appropriately stimulated. The second major change is toward an austerity program, taking mainly the form of a restrictive monetary policy designed to curb inflation and alleviate the balance of payment problem. This latter policy will presumably be transitory, to resolve a hopefully short run problem, whereas the shift in trade policy will be lasting.

These shifts create both problems and potential for small-scale enterprise. Some small scale industries fostered by the high protection of early years will be put at risk, and may collapse if the effective protection is reduced too quickly and they are unable to reduce costs enough to regain competitiveness in the domestic market. Others should be able to capitalize on the new directions of policy. Although parts of the primary sector are expected to be the main source of international competitiveness under the new directions, within manufacturing a number of small scale industries have export potential. But some interventions may be required for them to achieve their potential in this regard. While industries like clothing (some lines), leather work, and wooden furniture are both small scale and low cost, the small enterprise frequently faces special obstacles to exportation, including the cost of getting information about the process, the bureaucratic red tape, the

need for quality control, and the need for co-operation to achieve large enough supplies to be able to move into the international market. The foreign exchange bonanza of the 1970s both reduced the international competitiveness of such lines of manufacturing, and prevented any interest by the public sector in promoting them. In short, the industries in which the small-scale sector predominates are likely to have a high degree of actual or potential competitiveness in production but not in marketing and distribution. To the extent that they can enter world markets (and hold on to domestic ones) the benefits should go desproportionately to workers, these being labor intensive industries. If it is possible to facilitate the export process of small firms, they may eventually do better under an export oriented regime than under an import substituting one, since the latter type of regime tends to be (and appears in the Ecuadorean case to have been) designed to aid the larger, higher profile and better politically connected firms. Small industry benefits less from low priced machinery and raw material inputs since it uses less of them. It is less likely to reap the high monopoly profits possible for the large firm which has high protection against imports, since it competes against itself.

An austerity program can also be less damaging to the more self contained small enterprise than to the large one. It is probably true of all sectors of the economy that small firms receive less credit and other forms of outside assistance than to larger ones. While not condoning this as good practice, one can note that it may imply a greater resilience in the face of austerity. Again, however, that resilience may be helped along by certain complementary interventions; facilitating the organization of savings and loan co-operatives is one way, providing modest amounts of official-sector credit another, and so on.

When policy shifts are abrupt, as the two noted above have been (or will be), it is particularly important that small enterprise have the capacity to respond quickly to

the change of setting, and also have the capacity to make its voice felt in government.

## VII.- Conclusions and Policy Options

The characteristics of small enterprise (high labor intensity, limited use of imports, etc.), combined with the evidence of its significant contribution to Ecuador's development in recent decades, and with the nature of the current economic slowdown, suggests that it should retain a prominent and dynamic role in the country's economic evolution for the foreseeable future. For the country to achieve the maximum benefit from this sector, a number of constraints must be resolved, adjustments facilitated and latent potential released. As with other sectors, major importance attaches to getting the economy as a whole moving ahead at a satisfactory rate so that demand will be buoyant, expectations positive and so on. In this section we review the specific policy/program areas which need to be addressed on the economic side. These include matters of information, security (diminution of risk), access to resources at reasonable (i.e., not far from scarcity) prices, and freedom from unnecessary regulations, together with protection from possibly predatory activities from larger firms or government.

It is important to emphasize the need to assist the latent small business person as well as the already active one. In many sectors, the growth of employment in small enterprises comes more from the creation of new firms than the growth of existing ones. The present situation in Ecuador, given a modest further improvement in the overall performance of the economy, could be a good setting for the creation of many new enterprises. The recent marked decline in real wages (probably on the order of 25 percent for many groups between the peak in 1980 and the level of 1984) is likely to encourage many job holders to try to set up a business either as a side line or as a full time activity, in order to avoid such a sharp income cut <1>. Another group, unable to find work in the difficult labor market of today, will be induced to do the same. Whether these efforts are facilitated or impeded by public policy

will affect both the rate of growth of the economy and the levels of unemployment, poverty, and dissatisfaction.

The policy shift towards a greater export orientation creates both problems and opportunities for small scale enterprises. For some branches, it makes more urgent the need for flexibility --the capacity to adjust to new situations-- to avoid the cost implications of excessively expensive materials, capital, or labor. Thus, a number of policy/program improvements which would in any case have been desirable are now more urgent than before.

It is important to move, after due deliberation, towards an economic system in which rules are typically obeyed rather than circumvented. To achieve this would involve substantially decreasing the payoffs (i.e., incentives) to breaking rules, for example by trying to avoid excessive gaps between the official and the uncontrolled exchange rate, by making the labor code more feasible of fulfillment, by avoiding excessively low interest rates on credit, etc. It would involve setting less rules in the first place, where possible, and it would involve serious, forceful administration of those rules which are in fact necessary.

General assistance to the existing or budding entrepreneur, of whatever sort, is important. Information and other aids to adjustment are specially relevant to avoid a waste of built up entrepreneurial skills when changing economic conditions or a policy shift, such as that toward a more outward orientation, occur.

With respect to export encouragement and import protection, the small sector will clearly need better, more refined services in the future than it has had in the past. Continued study of effective protection rates for industry will be a needed input into upcoming and future changes in tariffs, to make sure that tariffs are

neither left unduly high nor lowered so brusquely as to eliminate potentially productive branches of industry. On the export side, the mechanisms of FOPEX and CATs ( Certificados de Abono Tributario ) will need to focus more vigorously on the small enterprise.

In more concrete terms, the policy options that should in our judgment be given maximum priority are the following:

1. A credit enhancement program must be implemented to improve accessibility to the small business sector, mainly manufacturing. The program must be designed and administered with the purpose of identifying the most entrepreneurial and efficient subjects. For cases involving promise but also excessive risk, loans can be made conditional on the borrower taking short practical training in administration technical skills adapted to his/her sector of activity. As large increases in credit availability to the small industry may be difficult, interest rates higher than the currently subsidized must be contemplated. The experience of PRODEM demonstrates that there are small entrepreneurs both willing to pay higher rates and at the same time able to invest the loans profitably. Positive real interest rates will also help to eliminate credit deviation towards uses of loans different from those originally intended, and could favor more productive investments on average.

2. Strategies to increase workers' productivity are desirable. The establishment of small skill and development centers can be implemented on an experimental basis first. If organized and managed under rigorous standards of excellence, they could soon become centers to which employers come looking for labor. Such centers could offer valuable opportunities to those willing to dedicate themselves to their personal development. Training programs could also promote future entrepreneurial skills in students who have the potential at some point to become self employed or

entrepreneurs.

3. Without conflicting with the previous point, existing skill development centers need to improve their linkages with the labor market and employers, thus fostering an appropriate focus on those skills most necessary in the working place. In spite of the many frustrations that the development of vocational training programs have suffered around the world, the fact remains that a well-trained worker is an indispensable component of the development processes. Many failures have been due to programs isolation from labor market, to poor selection of students and to lack of attention to attitudinal matters.

4. Additional skill development programs for entrepreneurs are needed. These could be designed in a variety of formats. Always starting small on an experimental basis, they could address basic skill needs, combining practical administrative skills with concrete technical components, as tailor-made as possible for specific sectors. This type of training could be linked to and complemented by the elements discussed in point one above. Other formats for entrepreneurial development could include basic instruction in warehousing, finances, marketing, management of personnel, etc. Chambers of Industry, CENAPIA and other institutions could play a significant role in identifying topics, sectors and geographic areas of priorities. These programs could develop into more formal consulting services for small businessmen or women, whether already established or new. The programs should attempt to recruit experienced business people (retired or still active) to participate in the transfer of knowledge and experience.

5. There are grave deficiencies in economic education in Ecuador. The gap created by lack of understanding by the general public on such basic issues as prices, supply and demand, productivity, salaries and similarly basic economic concepts, is

filled with ideological preconceptions. Emotional exchanges replace intelligent dialogues around economic and public issues in general. A public education campaign, using films in the style of the American Council in Economic Education, appropriately adapted to the Ecuadorean setting, could be of value at all ages and levels of the society. Such educational campaigns must be carried out systematically and over long periods of time.

6. A long-term strategy to deal with labor issues, in their many dimensions, is likely to become increasingly urgent. The current divisions in Ecuador between labor and capital are a pernicious and dangerous feature of the national scene as the economy enters a stage when misunderstanding and unwillingness to cooperate between these groups cannot be assuaged by the resources of an oil bonanza. These divisions constitute a real obstacle for future economic and social development, and for the political progress and stability of the nation. The politization of the labor movement and the perceived indifference by the entrepreneurial groups to the marginalization of workers can only be counteracted by a delicate action plan. Some of the components of such a plan have been mentioned above; point 5 is especially relevant. The development of better labor and business statistics (a major current failure of the public sector's information service) and the improvement of that public information system in general, as regards economic affairs (better trained economic journalists, etc.) could also contribute. A system of labor and business statistics to provide information on a regular basis about unemployment, wages, business successes and failures and the evolution of sales and investment by sectors and regions would help in reducing the uncertainty of business decisions, and in gaining a better understanding of the trends and capabilities of the economy.

7. The Ecuadorean public must be made aware that anybody with the energy and willingness to work hard stands a reasonable chance of becoming a successful

entrepreneur. This belief would help to coneract the pervasive notion that Ecuador is divided into two immutable and antagonistic classes. A public service of entrepreneurial advice, promotion and education could be established with this objective. Its central strategy would be to provide advice to protective entrepreneurs and to induce them to save and prepare themselves for a future venture. The service could be implemented through linkages with the banking community to offer savings mechanisms that could precede future credit and banking service for the would-be entrepreneur. It should also publicize the successes of the small self-made business man or woman and to promote the idea that "many people can make it." This approach can also help to popularize the idea that economic development in Ecuador fundamentally depends on its people, not the government.

8. The low quality of the Ecuadorean burocracy results partly from its size and partly from the low levels of compensation which result from budget constraints together with that large size. The previous point could provide a mechanism to reduce the size of the burocracy by offering a lump sum of money (or a fixed-term paid leave) to those public servants who would like to become independent entrepreneurs.

In the continous struggle to promote economic development, many recommendations have been offered, not a few of them imaginative and promising. The real test is in the "engineering" to implement them. Too many times good ideas have been killed by careless implementation. These policy options are no exception.

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## FOOTNOTES

### CHAPTER I

1. Few countries except large ones like Brazil or mineral rich ones have in fact been able to achieve high growth rates over extend periods without a significant contribution from small enterprise.
2. Banco Central del Ecuador. Programa de Encuestas de Coyuntura. Industria Manufacturera . No. 38. Enero 1985, página 2.
3. Ibid. Industria de Construcción . No. 39, página 3.
4. Based on the figures of Table A-3, allowing for the undercoverage of smaller establishments in each sector.
5. For the first two years total manufacturing employment is taken as the unadjusted census figure; non-small scale employment is based on the figures reported in INEC's Encuesta Anual de la Manufactura y Minería .
6. This is not, of course, to deny that there is plenty in Quito and Guayaquil also.

### CHAPTER II

1. The survey covered about two hundred small enterprises in the manufacturing sector in the cities of Quito and Guayaquil. See Annex C for details.

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### CHAPTER III

### CHAPTER IV

1. It does not include credit channelled to the public sector, since this is handled by the Development Bank (Banco de Desarrollo, BEDE). For 1982 BEDE held

10.3 percent of the total amount of outstanding loans (not credit flows) of the banking system in Ecuador. BEDE is not under the jurisdiction of the Central Bank and basically handles the financial needs of the central, provincial, and municipal governments and other government institutions and enterprises.

#### CHAPTER V

1. Sometimes, also, its quality is first rate, but since this situation implies that there is no problem to worry about, we will not deal with it here.

#### CHAPTER VI

1. It must be noted that it is in respect of the overall levels of government expenditures and revenues that fiscal policy is macroeconomic in nature; the composition of those expenditures and revenues, which in Ecuador is jointly determined by the Ministry of Finance, CONADE and the Congress, is, however, a sectoral dimension of fiscal policy and not a macroeconomic one.

2. The Ecuadorean Monetary Board is constituted by the following eleven members: The President of the Monetary Board, who is selected de facto by the President of Ecuador but formally appointed by Congress; the ministers of the following ministries: Finance, Agriculture, Natural Resources and Industry; the General Secretary of Planning from CONADE; one representative of the production chambers (Agriculture, Industry, Commerce and Construction) from the Coast and one from the Sierra; a representative of the private domestic banks; the "Superintendente de Compañías"; and the General Manager of the Central Bank. The chambers of small industrialists do not participate in the selection of representatives of the Monetary Board.

## CHAPTER VII

1. In Colombia there was a coincidence in timing between real wage declines of 15 to 20 percent for most categories of paid employees in the early 1970s (brought on mainly, it seems, by the acceleration of inflation) and the onset of very fast growth in the small manufacturing sector.

### ANNEX A

Tables cited in the text.

### ANNEX B

1. This Annex is based on the report prepared for AID in 1984 by Albert Berry, entitled "Employment and the Role of Intermediate Cities During the Coming Years". Further details are presented in that report.
2. World Bank, World Development Report , 1983
3. i.e. the percent of the population in the labor force.
4. The 1983 ISS-PREALC study of popular barrios in Quito and Guayaquil found a rate of 8.1 percent in Quito and 10.8 percent in Guayaquil for an average of 9.6 percent in the two cities (ISS-PREALC, Informe de Investigación sobre los Niveles de Vida de Barrios Populares y su relación con el Salario , Documento no Publicado, Quito, 1984). Since the unemployment rate tended percent for families with incomes under 8,000 sucres per month), the average for these cities as a whole would be less than than the 9.6 percent figure emerging from the study. Further, as noted by A. Gutierrez ( Empleo y Crecimiento , página 42) the definition of unemployment in this survey, "persons who could work but were not doing so" was broader than the

usual definition.

5. INEC, Estimación del Subempleo del Area Urbana del Ecuador y las Ciudades de Quito y Guayaquil, 1975 , Quito, INEC, 1979, página 33.

6. i.e. the number of completely unemployed persons who would correspond to the same total number of unworked hours (potential hours of work lost) as characterized this group.

7. The low incomes of many workers reflect a quite different dark side of the Ecuadorean reality --the extreme skewness in the distribution of income.

8. This figure is imprecise --see note to Table No. B-4.

Annex A

TABLE No. A-1

Occupied Economically Active Population in Urban Areas,  
by Economic Activity, and by Formal and Informal  
Sectors, 1980  
(Number of Persons)

Sector <sup>1/</sup>	Formal Employment		Informal Employment		Total	
	No.	%	No.	%	No.	%
1. Mining and Quarrying	3,411	100.0	-	-	3,411	100.0
2. Manufacturing Industry	126,017	77.1	37,485	22.9	163,502	100.0
3. Construction	60,524	75.0	20,175	25.0	80,699	100.0
4. Electricity, gas and water	10,500	100.0	-	-	10,500	100.0
5. a. Retail and Wholesale Trade	15,335	8.5	165,484	91.5	180,819	100.0
b. Restaurants and Hotels	25,493	56.4	19,739	43.6	45,232	100.0
6. Transport, Storage and Communication	21,610	43.8	27,727	56.2	49,337	100.0
7. Financial Services and Insurance Companies	28,768	100.0	n.a.	n.a.	28,768	100.0
8. Communal, Personal and Household Services	166,564	47.5	183,907	52.5	350,471	100.0
9. Other Activities	-	-	108,064	100.0	108,064	100.0
TOTAL	458,222	44.9	562,581	55.1	1,020,803	100.0

Source: Bastiaenen et al, "Urban Poverty", p. 65

1/ Excludes agriculture, forestry, fishing and hunting.

TABLE A-2

LABOR PRODUCTIVITY, REMUNERATION PER WORKER, AND OTHER CHARACTERISTICS OF ESTABLISHMENTS, CLASSIFIED BY NUMBER OF WORKERS:  
MINING, MANUFACTURING, COMMERCE, AND PRIVATE SECTORS SERVICES

Size of Establishments (Number of Workers)	Number of Establishments	Employed Workers		Paid Workers	Total Remuneration	Remuneration per Worker (000)	Value Added (Million)	Value Added per Worker (000)	Gross Investment (Millions)	Gross Investment per Worker (000)
		Number	Percent							
1 - 2	122,405	166,111	35.63	11,062	445.9	40.3	8,805	53.0	755.6	4.55
3 - 4	22,806	75,623	16.22	29,031	1,376.6	47.4	5,104	67.5	765.2	10.12
5 - 9	8,030	49,918	10.71	35,487	2,332.6	65.7	5,369	107.6	1,327.1	26.6
10 - 19	2,007	26,469	5.68	24,876	2,389.1	96.0	6,958	262.9	1,688.2	63.8
20 - 49	1,038	31,445	6.75	31,135	3,862.5	124.1	9,087	289.0	2,948.7	93.8
50 - 99	385	26,829	5.75	26,677	3,699.5	138.7	9,421	351.1	3,367.4	125.5
100 -199	195	26,558	5.70	26,306	3,946.1	150.0	9,746	367.0	4,659.9	175.5
200 -499	106	31,537	6.76	31,535	4,793.3	152.0	10,895	345.5	4,289.8	136.0
500 y más	32	31,702	6.80	31,702	4,449.6	140.4	43,357	1,367.6	6,870.1	216.7
	(31)	(31,143)		(31,143)	(4,266.4)	(137.0)	(8,810)	(282.8)	(3,560.9)	(114.3)
TOTAL	157,004 (157,003)	466,192 (465,633)		247,818 (247,259)	27,295.3 (27,112.1)	110.1 (109.7)	108,743 (74,196)	233.3 (159.3)	26,672.0 (23,362.8)	57.21 (50.17)

( ) Excluding production of crude petroleum and natural gas, which otherwise dominates the top size category though not being of any significance in the other categories.

**TABLE A-3**  
**SECTORAL DISTRIBUTION OF EMPLOYMENT AND VALUE ADDED BY SIZE OF ESTABLISHMENTS**

Size of Establish- ment (No. of Workers)	MANUFACTURING					COMMERCE					RESTAURANTS & HOTELS					OTHER SERVICES		
	Establ- ishments	Employment	Value	Added		Est.	Employment	Value	Added		Establ- ishments	Employment	Value	Added	Establishments	Employment		
1 - 2	22,091	30,944	16.55	1,919.1	5.04	71,064	94,934	54.93	4,758.6	27.59	13,838	20,118	41.55	1,067.5	30.79	15,391	20,065	35.98
3 - 4	7,394	24,870	13.28	1,783.1	4.68	8,274	26,841	15.53	1,759.8	7.87	3,722	12,388	25.58	670.8	19.35	3,392	11,439	20.57
5 - 9	2,959	18,479	9.87	2,040.1	5.36	2,005	12,657	7.32	1,654.4	7.40	1,519	9,308	19.22	632.6	18.25	1,516	9,263	16.61
10 - 19	915	12,155	6.49	1,796.5	4.72	650	8,574	4.96	2,689.5	12.02	184	2,320	4.79	251.4	7.25	248	3,276	5.87
20 - 49	525	16,009	8.55	3,587.1	9.42	320	9,545	5.53	3,839.7	17.17	61	1,824	3.77	232.0	6.69	121	3,737	6.70
50 - 99	235	16,327	8.72	4,654.6	12.23	83	5,890	3.41	2,414.3	10.79	14	942	1.95	126.5	3.65	50	3,508	6.29
100 - 199	127	17,641	9.42	5,446.4	14.31	46	6,335	3.67	3,116.3	13.93	3	424	0.88	139.5	4.02	19	2,158	3.87
200 - 499	83	24,674	13.18	9,043.5	23.76	13	3,618	2.09	1,097.1	9.90	3	1,095	2.26	346.2	9.99	6	1,744	3.13
500 and more	24	26,134	13.96	7,716.5	20.27	6	4,441	2.57	1,028.5	4.60	---	---	---	---	---	1	568	1.02
TOTAL RECORDED IN THE ECONOMIC CENSUS	34,355	187,249	100.00	38,064.8	100.00	82,461	172,834	100.00	22,368.0	100.00	19,344	48,419	100.00	3,466.5	---	20,711	55,762	100.00

SOURCES: INEC Censos Economicos 1980 Resumen Nacional Total de Establecimientos, Tomo 2, pp. 29-36

TABLE A-4

Trends in the Size Structure of the Manufacturing Sector

	1962	1974		1980	
Self-Employed <sup>a/</sup>	124,940	90,249	155,549	109,215 <sup>c/</sup>	157,215
2 - 4		39,700 <sup>b/</sup>		23,000	
5 - 9	40,780 <sup>d/</sup>	≈ 25,000	71,717	≈ 25,000	114,785
10 - 19		≈ 10,000		≈ 14,000	
20 - 49		≈ 12,000		16,009	
50 - 99		11,136		16,327	
more than 100		38,581		68,449	
Total	165,720 <sup>e/</sup>	226,266		272,000	

Note: Population census estimates of the total employment in manufacturing have not been adjusted upwards for undercoverage of the censuses. Such adjustment would in each case lead to a higher estimated share of employment in the smaller establishments.

<sup>a/</sup> Including Family Helpers.

<sup>b/</sup> If about 5000 employers, 9500 family helpers and 2000 others fall in this category, the remaining 23200 would be employees, probably too high, suggesting we may have overestimated the total number in this category.

<sup>c/</sup> A guess on the assumption that the job composition was the same as in 1974, as suggested by the overall figures of Table 7.

<sup>d/</sup> The Encuesta Manufacturera figure adjusted up by 12%; in 1974 our final estimate of the employment in plants of 10 or more workers was 8% above the total employment reported in the 1974 Encuesta.

<sup>e/</sup> Figure from ISS-PREALC, "Ecuador: Poblacion Economicamente Activa Corregida 1962-1974", Documento de Trabajo Q/8409, Borrador, March 1984, p.7. This is far below the original census figure, due to the conclusion (Ibid p.3) that there were differences of classification between the 1962 and the 1974 population censuses. The figure is designed to be comparable to that of 1974.

TABLE No. A-5

Size Structure of Urban Manufacturing<sup>a/</sup>, 1980, by Industry

	Number of Workers					Total
	1 - 4	5 - 9	10 - 19	20 - 49	≥ 50	
<b>Food, Beverages, Tobacco</b>						
Establishments	3,221	343	187	118	137	4,006
Workers	7,483	2,080	2,536	3,727	30,395	46,221
Percent of Workers	16.2	4.50	5.49	8.06	65.76	100.00
<b>Textiles, Clothing and Leather</b>						
Establishments	14,771	979	143	93	92	16,078
Workers	24,748	6,231	1,944	2,856	16,295	52,074
Percent (%)	47.52	11.97	3.73	5.48	31.29	100.00
<b>Wood &amp; Its Products</b>						
Establishments	5,966	639	144	44	34	6,827
Workers	11,684	4,021	1,840	1,316	5,218	24,079
Percent (%)	48.52	16.7	7.64	5.47	21.67	100.00
<b>Paper &amp; Printing</b>						
Establishments	550	201	64	45	31	891
Workers	1,267	1,224	835	1,396	4,776	9,498
Percent (%)	13.34	12.89	8.79	14.70	50.28	100.00
<b>Chemical &amp; Products of Petroleum, Coal, Rubber &amp; Plastic</b>						
Establishments	182	70	78	66	61	457
Workers	401	447	1,072	1,970	10,952	14,842
Percent (%)	2.70	3.01	7.22	13.27	73.79	100.00
<b>Non-Metallic Minerals</b>						
Establishments	1,295	181	81	30	29	1,616
Workers	2,714	1,072	1,168	942	50,73	10,969
Percent (%)	24.74	9.77	10.65	8.59	46.25	100.00
<b>Basic Metals</b>						
Establishments	25	6	9	3	10	53
Workers	51	47	118	110	1,269	1,595
Percent (%)	3.20	2.95	7.40	6.90	79.56	100.00
<b>Metal Products (inc. machinery workers)</b>						
Establishments	2,497	449	197	119	73	3,335
Workers	5,532	2,748	2,497	3,482	10,420	24,679
Percent (%)	22.42	11.13	10.12	14.11	42.22	100.00
<b>Other</b>						
Establishments	973	90	12	7	5	1,092
Workers	1,954	609	141	210	378	3,292
Percent (%)	59.36	18.50	4.28	6.38	11.48	100.00
<b>All</b>						
Establishments	29,485	2,953	915	525	472	34,355
Workers	55,834	18,479	12,151	16,009	84,776	107,249
Percent	29.82	9.87	6.49	8.55	45.27	100.00

a/ only a few rural establishments were included, these being the larger ones.

Source: Censos Económicos 1980, Resumen Nacional, Tomo 2, pp 30-33.

TABLE A-6

The Real Minimum Wage, 1968-1980  
(Sucre of 1970)

	(1)	(2)
1968	664	775
1969	632	737
1970	600	700
1971	684	798
1972	637	743
1973	568	663
1974	617	900
1975	675	979
1976	735	1041
1977	651	921
1978	575	815
1979	697	1016
1980	1236	1725
1981	1077	1503
1982	1080	1686
1983	886	1348
1984 (April)	822 a/	1227 a/
1984 (July)	689 b/	1029 b/
1985 (March)	731 c/	1092 c/

a/ Based on prices of April 1984

b/ Based on prices of July 1984

c/ Based on prices of March 1984

Note: The figures are based on a deflation of the highest minimum wage occurring in a given year by the national cost of living series (which refers to middle and low income" families) for that year. Since food prices have recently risen substantially faster than other prices, the real wage will have moved less positively than indicated here for those within above average expenditure falling in this category.

(2) Refers to a person who received the extra months of salary as they entered the legislation as well as the Bonificación Complementaria introduced in 1974 and the cost of living allowance introduced first in that year and increased in 1982.

Transportation allowance and other payments not generalized to all workers are not taken into account.

Employees clearly differ in terms of how the legislation impinges on them. For the figures referring to April 1984 and on, it is assumed that the relation between Col (2) and Col (1) remains constant at the level of April 1984.

TABLE No. A-7

VOLUME OF CREDIT GRANTED BY THE ECUADOREAN BANKING AND FINANCIAL SYSTEM BY SECTORS  
(In millions of current sucres)

	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982
<u>MANUFACTURING</u>	2,443	3,027	4,454	6,647	9,050	12,184	16,563	22,488	32,945	44,464	61,707
Large Industry	2,264	2,767	3,579	5,547	7,254	10,163	14,436	19,907	30,137	40,609	56,978
Small Industry & Art (SIA)	179	260	876	1,100	1,795	2,022	2,127	2,581	2,808	3,855	4,731
<u>NON-MANUFACTURING</u>											
Agriculture	2,044	2,791	4,830	6,924	8,035	9,240	11,543	13,911	18,955	25,594	30,618
Commerce	8,344	9,864	12,214	15,017	19,001	21,944	24,057	32,507	42,031	53,897	62,387
Others	1,609	1,804	3,948	4,529	5,478	7,414	8,902	10,633	15,603	25,721	32,025
<u>TOTAL</u>	14,441	17,448	25,446	33,117	41,564	50,784	61,065	79,541	109,535	149,676	186,737
<u>PERCENTAGES</u>											
SIA's share of total	1.24	1.49	3.44	3.32	4.32	3.98	3.48	3.25	2.56	2.58	2.53
SIA's share of Manufacturing	7.33	8.60	19.66	16.54	19.84	16.59	12.84	11.48	8.52	8.67	7.66
Manufacture's share	16.92	17.35	17.51	20.07	21.77	23.99	27.12	28.27	30.08	29.71	33.04

SOURCE: Banco Central del Ecuador (Prepared by CENAPIA)

TABLE A-8

IMPORTS BY SMALL INDUSTRY AND ARTISANRY AND THE FISCAL SACRIFICE OF TARIFF EXEMPTIONS

1974 - 1984.

(Millions of sucres)

<u>YEAR</u>	<u>MACHINERY</u>		<u>RAW MATERIALS</u>	
	<u>CIF VALUE</u>	<u>FISCAL SACRIFICE</u>	<u>CIF VALUE</u>	<u>FISCAL INCENTIVES</u>
1974	35'517	4'873	8'102	935
1975	42'257	5'477	7'765	1'351
1976	93'797	13'328	42'845	14'516
1977	112'024	12'919	87'636	17'452
1978	176'885	28'805	153'530	39'524
1979	154'713	25'612	198'129	37'720
1980	51'136	11'461	50'488	9'293
1981	96'065	13'047	72'531	7'951
1982	39'012	7'025	82'530	18'838
1983	33'059	6'559	80'318	13'670
1984	27'403	2'312	133'393	15'033

SOURCE: MICEI. Dirección de Pequeña Industria. Departamento Estadístico.

Annex B <1>

Employment Patterns in the 1970s and the 1980s

GNP in Ecuador grew rapidly at 8.6 percent per year over 1970-1981, as the petroleum boom fuelled a rapid expansion of the modern sector in general, and especially of urban based activities. Manufacturing output grew at an average of nearly 11 percent per year, while agriculture grew at a little under 3 percent <2>. Population was probably rising at something under 3 percent per year so per capita output was rising at nearly 6 percent per year and per capita income at an even faster rate due to the favorable shift in the country's international terms of trade.

Ecuador pursued a dualistic development strategy during the 1970s, focussing on the modern sector as the main motor for growth. The major block of financial resources and a disproportionate amount of human resources were involved in pushing larger scale manufacturing, commercial agriculture, large public works infrastructure projects and so on. With the wealth of oil revenues available, the degree of capital investment was very large, and although a more efficient and equitable pattern of growth could have been pursued, the evidence does suggest that the benefits of growth were spread fairly widely. In the absence of such resource and foreign exchange surpluses, such a strategy could lead to falling incomes for significant parts of the population.

Several features of the 1970s contributed to an apparently relatively smooth process of growth cum rapid urbanization, smooth in the sense that unemployment never reached high levels, nor was there serious evidence that large groups were suffering income losses or finding their aspirations seriously blocked. Most notable were the

increasing demand for labor in the modern urban economy and the only modest increase in the total (rural plus urban) labor force.

The growth of the labor force during the 1970's, and in particular over the 1974-1982 intercensal period for which fairly detailed data are available, was not excessive -- about 2.5 percent per year-- despite the fast growth of the population in the working age category, which for persons 15 years and up was of about 3 percent per year. The key here was that the participation rate for the population as a whole <3> stayed constant --29.8 percent in 1974 and 29.7 percent in 1982 (unadjusted figures); that for persons 15 and up fell from 51.5 percent to 49.4 percent, due mainly to considerable declines in the younger age groups, for males of 15-24 years especially. The main cause of the decline in the male participation rate, and a factor which probably prevented the female participation rate from rising faster than it did, was the increase in the percent of youth 15 and up who were studying . This increase in persons studying corresponded to a decrease of perhaps 3.5 percent in the participation rate of person 12 and up.

One may safely surmise that growth on the labor supply side will not continue to be so moderate. Although the gradually falling rate of population growth will eventually tend to slow the expansion of the supply of labor, this will take a while to show up strongly. Meanwhile a continued decrease in the participation rate cannot be expected; rather the participation rate for women aged 20 and up will presumably continue to increase, following the normal pattern in the middle stages of economic development as urbanization proceeds, and is likely to more than offset further increases in the share of persons 15 and up who are full time students. Thus the temporary easing of supply side pressure in the labor market is likely to be reversed soon, if it has not already been.

The relatively rapid population growth of the principal two cities and most of the

secondary cities (see Table B-1) appears to have led to a nearly constant rural population during the intercensal period 1974-1982. The urban population grew at about 5 percent --fast but less than has often characterized the rapidly growing cities of Latin America. The secondary cities grew on average at about the same rate as greater Quito and Guayaquil, though there was much variation from city to city; Ibarra grew by 28 percent while Santo Domingo de los Colorados grew by 120 percent.

The sectoral structure of the labor force in Ecuador changed rather sharply over the boom period since the early 1970s, with agriculture's share falling by over 10 percent in eight years following on a decline of 10 percent over the previous 12 years (Table No. B-2). In the urban labor force, services registered an increase in share while both agriculture and manufacturing fell (Table B-3)

The share of the labor force working for a wage (or salary) was about 53 percent in 1982 --up marginally from about 51 percent in 1974 and 48 percent in 1962. In the urban areas, however, the figure fell from 67 percent in 1974 to 63 percent in 1982 as the self employment and employer categories both rose a little, in spite of a shift in the composition of the urban labor force toward sectors with an above average share of workers who are paid--construction, transportation, finance and other services.

According to the available figures the labor force in urban Ecuador has not been characterized by a high degree either of open unemployment or of underemployment, at least until the last two or three years. This is consistent with the evidence of considerable job creation and wage increases during the 1970s. The relatively low rates of open urban unemployment reported in the 1970's may owe something also to the high degree of inequality of income distribution in Ecuador, resulting in a

tendency for most job seekers not to wait long before moving into the informal sector and/or not to migrate to an urban area unless reasonably sure of some sort of work.

The observations on open urban employment over 1968-1975 lay in the range 4.4 percent to 5.5 percent, with a significant portion in each case being accounted for by first job seekers. By November 1982 the population census figure had reached 6.9 percent, and it is widely believed, though the statistical evidence is partial, that open unemployment is considerably higher now, and evidence from Quito and Guayaquil suggests rates of 15 percent for poor families <4>. In urban samples for 1968 and 1975 underemployment was estimated to be high (30 percent and 24 percent respectively) <5> but the bulk of the "underemployed" persons were so classified either because they had low incomes or were working in jobs where, judged by the current patterns in Ecuador, their educational qualifications were excessive; persons working less than they wanted to were few, and the full person equivalent unemployment <6> was probably only 1-2 percent of the labor force. In short, these surveys provide no persuasive evidence of significant levels of underutilization of labor at the time <7>. This is not to say that the serious underutilization has not existed, only that the available measures have not been appropriate to capture it. Probably the major underutilization has been in such sectors as the government (some branches), retail commerce, and the like. People work at a slow pace but because their incomes are not atypically low they are not classified as underemployed in surveys like those taken in Ecuador.

The unusually low levels of unemployment and measured underemployment (by the standards of Latin countries at least) have almost certainly changed significantly for the worse since 1982, as noted above. And the distribution of unemployment across the population may also be changing. As of 1975, the rate of unemployment

bore the usual negative relation with age, falling from 13 percent for persons 15-19 to 1-2 percent for those 30 and up. And it was also typical in being higher for persons with a secondary level of education than for those with either lower or higher levels, suggesting though not demonstrating that unemployment may have been lower among the poor households than among better off ones. The high rates observed in the lower income barrios of Quito and Guayaquil in 1983 suggest that the unemployment problems of the poor may have worsened faster than those of the rich.

The employment trends of the 1970s boom period witnessed a considerable expansion of modern sector employment, if this be defined as including establishments above a certain size (number of workers) as well as self-employed professionals and public sector employees. And wages for most of the modern sector occupational categories showed quite positive trends.

The major sources of new jobs in urban areas between 1974 and 1982 were private sector services (commerce, restaurants, personal services, etc) with 36 percent, public sector employment with as much as a third <8> manufacturing with 16 percent and construction with a striking 13 percent in the smaller urban areas. Public sector employment also seems to have been important in most urban centers. The fact that, between them, the recently stagnant construction sector and the public sector appear to have created around 45 percent of the new jobs over this period highlights the challenge of job creation in the near future, when the public sector cannot be counted on for many if any new jobs and when construction employment is only likely to rise to the extent that it is stimulated by the government.

A striking feature of Ecuador's job market is the high and rising level of education of the labor force. For its level of per capita income, Ecuador has long had unusually high levels of educational achievement, at least as defined by the grade

reached. These levels continued to increase during the last couple of decades; already rather high in 1974 they were extraordinary for the younger cohorts by 1982 (Table B-5). The last decade or so has witnessed a particularly rapid growth of enrollment in higher education, at around 20 percent per year over the 1970s. In the urban areas, of the age group (cohort) now in secondary school probably around 30 percent will end up with higher education (a majority of these having 4-6 years) and another 40 percent will have secondary school (partial or complete).

Education is sought with great determination in Ecuador, as in most developing countries, because of the high perceived pay-off to the recipient. As of 1975 in urban Ecuador the typical (median) person with four to six years of higher education earned over 6.5 times as much as the average person without education. Such a differential --observed also in other developing countries with highly unequal income distributions, naturally puts great pressure on parents to educate their children. It helps to explain the high incidence of work cum study in Ecuador; as of 1974 over 15 percent of persons 15 - 24 in the labor force were also studying . And it explains why so many people are still studying, at least part time, into their mid-twenties.

TABLE B-1

Population Growth 1974-82, by Size of Urban Center in 1982

	1974		1982		Percent Increase in Population 1974-82
	Population	Percent of Total Population	Population (Thousands)	Percent of Total Population	
1. Metropolitan Areas					
Guayaquil	852	12.5	1243	15.4	45.9
Quito	714	10.5	1034	12.8	44.8
Cities of 200,000- 500,000		none			
Cities of 100-200 <sup>a/</sup>	310	4.5	460	5.7	48.4
Cities of 20-100 <sup>b/</sup>	597	8.7	888	11.0	48.7
Cities of 10-20	165	2.4	289	3.6	75.2
Towns of 5-10	196	2.9	223	2.8	13.8
Towns of 2-5	202 <sup>c/</sup>	3.0	259	3.2	28.2
Urban	3036	44.4	4396	54.5	44.8
Rural	3794	55.6	3677	45.5	declined <sup>d/</sup>
Total	6830	100.0	8073	100.0	18.2

a/ Cuenca, Machala, Portoviejo, Ambato.

b/ 17 cities.

c/ many of these had less than 2,000 people in 1974.

d/ Probably the rural population was in fact about constant. See the discussion under "Sources".

Source: Progress Report for the Ecuador Project on Urban-Rural Linkages, Appendix A. Note that the 1974 figures include an upward adjustment for undercoverage whereas those for 1982 do not; hence there is some understatement of all growth rates, probably especially for the rural areas.

Table B-2

Percent Distribution of the Labor Force by Sector  
1962, 1974 and 1982

	1962	1974	1982
Agriculture et al	63.0	52.9	42.5
Mining	0.2	0.3	0.3
Manufacturing	9.4	10.2	10.4
Public Utilities	0.2	0.4	0.5
Construction	2.8	3.9	5.7
Commerce, Restaurants, Hotels	5.8	8.5	9.6
Transport	2.5	2.5	3.7
Finance	0.6	0.9	1.4
Services	13.2	14.8	21.9
Not Specified	2.5 <sup>b/</sup>	5.6 <sup>b/</sup>	4.1 <sup>b/</sup>

b/ includes first job seekers.

Source: Adjusted census figures from Gutierrez, Empleo y Cre-  
cimiento p.30.

Note that the share of the labor force in agriculture is higher than in the unadjusted census figures, which were judged to have included too few women. This and other changes are discussed in the source and the references cited therein.

TABLE B-3

Composition of the Urban Labor Force by Sector  
1974 and 1982

	<u>1974</u>		<u>1982</u>	
	Number	Percent <sup>a/</sup>	Number	Percent <sup>a</sup>
Primary				
Agriculture and Mining	66,033	8.73	69,759	5.97
Secondary	199,760	26.43	301,635	25.30
Manufacturing	135,241	17.90	188,551	16.13
Construction	58,286	7.71	102,144	8.74
Public Utilities	6,233	0.82	10,940	0.94
Tertiary	489,844	64.83	797,740	68.23
Commerce, etc.	153,484	20.31	218,187	18.66
Transportation, etc	42,662	5.65	76,034	6.50
Finance, etc	19,374	2.56	36,426	3.12
Other services	274,324	36.31	467,093	39.95
TOTAL	733,350	100.00	1169,134	100.00

<sup>a/</sup> Of those reporting sector of activity.

Source: For 1974, the adjusted data presented interalia in Banco Central del Ecuador Boletín Anuario No. 7 1984, p. 192. For 1982, the unadjusted figures of INEC, Resultados Anticipados.

TABLE B-4

New Urban Job Creation by Sectors, 1974-82

Sector	Employment in 1974	Employment in 1982	Change 1974-82	
			Absolute	%
Agriculture et al	61,047	66,900	5,853	1.63
Manufacturing	131,119	188,551	57,432	16.02
Construction	56,014	102,144	46,130	12.87
Services, Public				
Utilities, Mining	562,508	811,539	249,031	69.48
(i) Public Sector (I)		263,563 <sup>d/</sup>		
(II)	≈130,000 <sup>b/</sup>	≈250,000 <sup>a/</sup>	120,000	33.40
(ii) Rest	432,509 <sup>c/</sup>	561,539 <sup>c/</sup>	129,030	36.00
Total	810,689	1169,134	358,445	100.00

Sources: The 1974 population census and the 1982 advance sample, plus those indicated in the footnotes.

- a/ Extrapolated from the figure of 236,340 for 1981, cited in Gilda Farrell, Mercado de Trabajo Urbano y Movimiento Sindical, Quito, IIE-PUCE-ILDIS, 1982 p.59. Some of these people would be located in rural areas. Presumably members of the armed forces are included.
- b/ Based on the 1975 figure of 150,552 (Junta Nacional de Planificación, Primer Censo Nacional de Servicios Públicos 1975, Resultados Provisionales) and G. Farrell's observation that the number of workers in public administration quadrupled over the 1970s (G. Farrell, Los Trabajadores Autonomos de Quito, Quito, ILDIS-IIE-PUCE, 1983 p63).
- c/ All of "services et al" minus estimate (ii) of public sector employment.
- d/ From the population census; the source of divergence with estimate (ii) is not known.

TABLE B-5

## Educational Levels in Urban Areas, by Age, 1982

Age	None	Literacy Center	Primary		Secondary		Higher	
			1-3	4-6	1-3	4-6	1-3	4-6
10-14	3.03	0.17	21.06	55.23	20.51	-	-	-
15-19	2.44	0.45	5.02	25.16	38.14	26.54	2.25	-
20-24	3.22	0.44	4.59	25.68	21.45	25.55	15.48	3.59
25-29	4.03	0.51	5.88	29.61	18.32	18.16	11.90	11.62
30-34	5.47	0.74	8.78	34.75	15.54	16.29	7.11	11.32
35-44	9.03	0.82	11.69	39.74	13.20	13.52	3.51	8.48
45-54	13.26	0.56	15.44	42.13	10.04	11.31	2.10	5.05
55-64	18.73	0.41	16.11	41.03	8.93	9.48	1.60	3.71
Total (and up)	6.82	0.48	10.83	36.36	19.73	15.41	5.57	5.13

a) Persons not declaring their level of education are excluded.

Source: INEC, Resultados Anticipados, p.25.

ANNEX C

ESTIMATES OF THE SHARE OF THE LABOR FORCE EARNING LESS THAN THE MINIMUM WAGE

1. For 1975, assuming an approximately 45% addition to the basic minimum wage to allow for fringe benefits, it was 21.9 thousand sucres per year. In urban areas, according to the income distribution presented in Berry 1984, the 42.8 percent of earners were below 24,000; thus about 40 percent were below the minimum wage. Thus about 42-43 percent of workers, including unpaid family helpers, fell below this cut off line.

If rural income were half as high and had the same distribution as urban income, about 70 percent of workers would be below this level (based on the distribution just cited). If the population was 55 percent rural and 45 percent urban, the share of all workers falling below the urban minimum wage is 57-58 percent. If one includes only remuneration, the figure would be somewhat higher since the income distribution figures used in these calculations include also non-labor income. On the other hand if those figures were generally downward biased, this would work in the opposite direction.

2. For 1982, assuming the same distribution of income as in 1975, a growth of the labor force of 25 percent per year and using the Central Bank figures on "ingreso disponible bruto de hogares por habitante" ( Cuentas Nacionales 1984 , pagina 26) as the evidence on income growth, but converted to income per active person, and assuming the overall distributions of income to be the same in 1982 as 1975, the share of workers falling below that years minimum wage would be about 55 percent.

ANNEX D

THE SURVEY OF SMALL INDUSTRY, APRIL 1985

This survey was designed and carried out to produce some updated material for this study. It consisted of a stratified sample of 200 observations. The strata were defined in terms of two geographic areas: Quito and Guayaquil and five industrial sectors in both cities. The chosen sectors were:

- a) Food products, excluding beverages
- b) Clothing (excluding shoes)
- c) Wood Products (especially furniture)
- d) Non-Metallic mineral products (Construction Materials)
- e) Metal Products, Machinery and Electrical Equipment.

Each sample unit was selected randomly within each stratum using diverse directories. A copy of the questionnaire is attached.

1. INFORMACION GENERAL

- 1.1 Nombre de la empresa (razón social) \_\_\_\_\_
- 1.2 Nombre de la persona entrevistada \_\_\_\_\_
- 1.3 Dirección de la empresa  
Calle \_\_\_\_\_ No. \_\_\_\_\_  
Ciudad \_\_\_\_\_ Telf: \_\_\_\_\_
- 1.4 Hace cuantos años comenzó a operar el negocio? \_\_\_\_\_

2. RELACIONES DE LA EMPRESA

- 2.1 De cuáles asociaciones gremiales o de su rama es usted miembro?

Cámara de Pequeños Industriales  
Otra \_\_\_\_\_

- 2.2 Conoce usted lo que hacen las instituciones siguientes?  
Ha recibido algún beneficio de ellas en los últimos dos años?

	CONOCE	RECIBI BENEFICIOS
MICEI	_____	_____
CENAPIA	_____	_____
SECAP	_____	_____
CENDES	_____	_____
FOPINAR	_____	_____
INEN	_____	_____
CEBCA	_____	_____
FOPEX	_____	_____
OCEPA	_____	_____

- 2.3 De que fuentes su empresa ha recibido financiamiento en los dos últimos años?

- 0. Nunca hemos recibido financiamiento \_\_\_\_\_
- 1. Prestamistas privados \_\_\_\_\_
- 2. Banco de Fomento \_\_\_\_\_
- 3. Cooperativas de ahorro y crédito \_\_\_\_\_
- 4. Bancos comerciales \_\_\_\_\_

3. MERCADO Y VENTAS

- 3.1 Qué porcentaje aproximadamente de sus Ventas va a:  
El público (individuos) \_\_\_\_\_  
La empresas o instituciones privadas \_\_\_\_\_  
El gobierno o las empresas públicas \_\_\_\_\_

- 3.2 Qué porcentajes de sus Ventas van a cada área? 100%

La misma ciudad \_\_\_\_\_  
Otras áreas del país \_\_\_\_\_  
Al extranjero \_\_\_\_\_  
100%

- 3.3 Cuántos competidores conoce usted que se hayan arruinado desde 1.980?

- 3.4 Cuáles han sido las principales causas de las quiebras?

Mala situación económica general \_\_\_\_\_  
Mala administración de la empresa \_\_\_\_\_  
Falta de crédito \_\_\_\_\_  
Falta de materias primas o insumos \_\_\_\_\_  
Competencia de importaciones o contrabando \_\_\_\_\_  
Otras \_\_\_\_\_

- 3.5 Qué porcentaje de su industria estima usted que se ha arruinado desde 1.980? \_\_\_\_\_ %

- 3.6 Su competencia proviene principalmente de:  
(Por favor marque los dos más importantes)






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- 1. Otros pequeños industriales \_\_\_\_\_
- 2. Gran industria privada \_\_\_\_\_
- 3. Empresas estatales \_\_\_\_\_
- 4. Importaciones y contrabando \_\_\_\_\_
- 5. No tengo competencia para algunos de mis productos \_\_\_\_\_
- 6. No tengo competencia alguna \_\_\_\_\_
- 3.7 Indique los montos de ventas anuales en 1.980 y 1.984
- SUCRES

	1.980	1.984
Menos de un millón	_____	_____
De 1 a 5 millones	_____	_____
De 5 a 10 millones	_____	_____
De 10 a 20 millones	_____	_____
De 20 a 50 millones	_____	_____
Mas de 50 millones	_____	_____

- 3.8 Cómo se hacen las ventas?

  - Los clientes vienen a la empresa \_\_\_\_\_
  - Envío vendedores a los clientes \_\_\_\_\_
  - Hago publicidad \_\_\_\_\_
  - Busco clientes grandes y distribuidores \_\_\_\_\_
  - Otra \_\_\_\_\_

- 3.9 Cuando usted ofrece un nuevo producto o abre un nuevo mercado, su decisión se basa en:

  - Pedidos de los clientes \_\_\_\_\_
  - Lo que observó de los competidores \_\_\_\_\_
  - Ideas que se me ocurren o leo \_\_\_\_\_
  - Sugerencias de trabajadores o amigos \_\_\_\_\_
  - Estudios de mercado \_\_\_\_\_
  - Otros \_\_\_\_\_

- 3.10 Desea usted vender mucho más?

1. SI \_\_\_\_\_ 0. NO \_\_\_\_\_

- 3.11 Qué le permitiría vender más? (Por favor marque las tres más importantes)

  - 1. Una mejor situación económica general \_\_\_\_\_
  - 2. Más disponibilidad de crédito \_\_\_\_\_
  - 3. Ayuda en la promoción de mis productos \_\_\_\_\_
  - 4. Más facilidad para vender al gobierno \_\_\_\_\_
  - 5. Menos trabas burocráticas oficiales \_\_\_\_\_
  - 6. Reducir las exigencias y garantías de crédito \_\_\_\_\_
  - 7. Mayor disponibilidad de materias primas e insumos \_\_\_\_\_
  - 8. Disminución de importaciones competitivas y contrabando \_\_\_\_\_
  - 9. Facilidades para exportar \_\_\_\_\_
  - 10. Que el estado me ayude \_\_\_\_\_
  - 11. Que el estado interfiera menos \_\_\_\_\_
  - 12. Otras \_\_\_\_\_

- 3.12 Qué expectativas tiene usted en cuanto al futuro de su empresa en los próximos dos o tres años?

  - 4. Los negocios van a mejorar \_\_\_\_\_
  - 3. Los negocios continuarán igual \_\_\_\_\_
  - 2. Los negocios van a empeorar \_\_\_\_\_
  - 1. No sé lo que va a pasar \_\_\_\_\_
  - 0. Puede que abandone el negocio \_\_\_\_\_

- 3.13 Durante los próximos seis meses planea usted:

  - Invertir más capital en la empresa \_\_\_\_\_





--



Sacar un nuevo producto \_\_\_\_\_  
 Contratar más empleados \_\_\_\_\_  
 No sélo que haré \_\_\_\_\_

4. EMPLEO Y ENTRENAMIENTO

4.1 Cuántos empleados y obreros tenía su empresa cuando comenzó y cuántos tiene ahora?

	COMIENZO	AHORA
PERMANENTES	_____	_____
TEMPORARIOS	_____	_____
TOTAL	_____	_____
FAMILIARES	_____	_____
SIN SUELDO	_____	_____

4.2 Del total actual, cuántos son calificados o no calificados?

CALIFICADOS \_\_\_\_\_  
 SEMI CALIFICADOS \_\_\_\_\_  
 NO CALIFICADOS \_\_\_\_\_

4.3 Del total actual, cuántos han sido entrenados por:

La propia empresa \_\_\_\_\_  
 SECAP \_\_\_\_\_  
 CENAPIA \_\_\_\_\_  
 Cámara de Pequeños Industriales \_\_\_\_\_  
 Otra \_\_\_\_\_

4.4 La capacitación recibida de las instituciones ha sido más valiosa en:

1. La parte teórica \_\_\_\_\_  
 2. La parte práctica \_\_\_\_\_  
 3. Ambas \_\_\_\_\_  
 4. Ninguna \_\_\_\_\_

4.5 Existe comité de empresa en su negocio?

1. SI \_\_\_\_\_ 0. NO \_\_\_\_\_

4.6 De lo que usted gasta en subcontratación, qué porcentaje representa este rubro en las ventas totales? \_\_\_\_\_

4.7 Si sus Ventas aumentasen mucho usted: (Por favor marque una sola respuesta)

1. Contrataría más personal permanente? \_\_\_\_\_  
 2. Contrataría más temporales \_\_\_\_\_  
 3. Aumentaría las horas extras \_\_\_\_\_  
 4. Subcontrataría trabajos para hacerse fuera de la empresa \_\_\_\_\_  
 5. Otra \_\_\_\_\_

4.8 (Si marca 3, 4 o 5 arriba) Porqué no contrataría más personal permanente o temporal?

El salario mínimo es demasiado alto \_\_\_\_\_  
 No quiero un comité de empresa \_\_\_\_\_  
 Otra \_\_\_\_\_

5. INNOVACIONES

5.1 Hace cuántos años instaló usted nueva maquinaria?

1. Hace un año o menos \_\_\_\_\_  
 2. Entre uno y dos años \_\_\_\_\_  
 3. Entre dos y cuatro años \_\_\_\_\_  
 4. Hace más de cuatro años \_\_\_\_\_

5.2Cuál fue el propósito?

Reemplazar equipo viejo \_\_\_\_\_  
 Aumentar la producción \_\_\_\_\_  
 Mejorar la calidad del producto \_\_\_\_\_  
 Hacer nuevos productos \_\_\_\_\_  
 Producir más sin aumentar \_\_\_\_\_












personal \_\_\_\_\_  
Otras \_\_\_\_\_

5.3 Qué requeriría para modernizar su empresa?  
(Por favor marque la más importante)

- 1. Más capital \_\_\_\_\_
- 2. Mejor asistencia técnica \_\_\_\_\_
- 3. Que aumenten las Ventas \_\_\_\_\_
- 4. No necesito modernizar \_\_\_\_\_
- 5. Otra \_\_\_\_\_

6. INFORMACION COMPLEMENTARIA

6.1 Es el local propio de la empresa o empresario?

- 1. SI \_\_\_\_\_ 0. NO \_\_\_\_\_

6.2Cuál es la situación jurídica actual de la empresa?

- 1. Unipersonal \_\_\_\_\_
- 2. Sociedad de hecho \_\_\_\_\_
- 3. Compañía limitada \_\_\_\_\_
- 4. Compañía anónima \_\_\_\_\_
- 5. Cooperativa \_\_\_\_\_
- 6. Otra \_\_\_\_\_

6.3 Cómo comenzó el negocio?

- 1. Heredando \_\_\_\_\_
- 2. Comprando \_\_\_\_\_
- 3. Fundando \_\_\_\_\_

6.4 Cómo fue financiado el negocio inicialmente?

- 1. Con capital de los dueños \_\_\_\_\_
- 2. Con préstamos privados \_\_\_\_\_
- 3. Con financiamiento bancario \_\_\_\_\_
- 4. Otro \_\_\_\_\_

6.5 Conoce usted la Ley de Fomento de la Pequeña Industria?

- 1. SI \_\_\_\_\_ 0. NO \_\_\_\_\_

6.6 Indique donde está su empresa registrada

Superintendencia de Compañías \_\_\_\_\_  
 Tiene número patronal del IESS \_\_\_\_\_  
 Clasificación del MICEI \_\_\_\_\_  
 Calificación del MICEI \_\_\_\_\_

6.7 Cuántos meses duró el trámite para calificarse con el MICEI?

6.8 Ha mejorado la situación de su empresa como resultado de esa ley?

- 1. SI \_\_\_\_\_ 0. NO \_\_\_\_\_

6.9 Se siente usted identificado con la labor del FENAPI?

- 1. SI \_\_\_\_\_ 0. NO \_\_\_\_\_

6.10 Qué institución provee más apoyo a su empresa?

- 1. MICEI \_\_\_\_\_
- 2. CENAPIA \_\_\_\_\_
- 3. FENAPI \_\_\_\_\_
- 4. SECAP \_\_\_\_\_

6.11 Qué tres servicios o formas de asistencia desearía recibir para mejorar su empresa?

\_\_\_\_\_

6.12 Si usted tuviera este momento un millón de sucres, lo invertiría en su negocio?

- 2. SI \_\_\_\_\_ 1. NO SE \_\_\_\_\_ 0. NO \_\_\_\_\_

7. INFORME DEL ENTREVISTADOR  
(Para completar después de la entrevista)

7.1 Nombre de la Empresa \_\_\_\_\_

7.2 Número de la entrevista Nº 325

7.3 Sector o Rama \_\_\_\_\_

7.4 Fecha de la entrevista \_\_\_\_\_  
DIA MES AÑO

7.5 Duración de la entrevista: \_\_\_\_\_ minutos

7.6 Sexo del empresario: 1. Masculino \_\_\_\_\_ 0. Femenino \_\_\_\_\_

7.7 Edad del empresario (a)

- 1. Hasta 30 años \_\_\_\_\_
- 2. De 30 a 50 años \_\_\_\_\_
- 3. Más de 50 años \_\_\_\_\_

7.8 Confiabilidad de las respuestas

- 0. Nada confiable \_\_\_\_\_
- 1. Algo confiable \_\_\_\_\_
- 2. Bastante confiable \_\_\_\_\_
- 3. Muy confiable \_\_\_\_\_

7.9 Grado de cooperación

- 0. Bajo \_\_\_\_\_
- 1. Regular \_\_\_\_\_
- 2. Bueno \_\_\_\_\_
- 3. Muy bueno \_\_\_\_\_

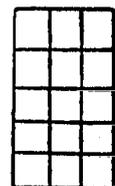
7.10 Entendimiento de las preguntas

- 0. Malo \_\_\_\_\_
- 1. Regular \_\_\_\_\_
- 2. Bueno \_\_\_\_\_
- 3. Muy bueno \_\_\_\_\_

7.11 Comentarios sobre las preguntas no confiables.  
(Identifique el número de las preguntas específicas)

\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

Entrevista hecha por: \_\_\_\_\_ / /  
Codificación hecha por: \_\_\_\_\_ / /  
DIA MES AÑO



## ANNEX E

### Notes on Problems and Prospects of Small Manufacturing Enterprises in Quito and Guayaquil, 1985

The economic slowdown of the 1980s is believed by many to have impacted more strongly on the small industry sector than the large scale sector and perhaps also than Artisanry. Unfortunately no satisfactory data are available to allow a judgment at this point. If we judge by the number of firms newly registering, under the small Industry and Artisan Development Law, this would appear to be the case. Whereas in the mid 1970s (1974-1978) more than 200 firms register each year (average of 270), the average over 1982-1984 was only 79 firms. A similar decline occurred in the case of large firms registering under the Industrial Development Law; whereas an average of 73 firms registered during the years 1973-1976, that for 1982-1984 was only 37. Responses from 200 small manufacturing enterprises interviewed in Quito and Guayaquil.

The entrepreneurs in our survey have provided us with useful information on the problems, prospects and characteristics of the sector. The evolution of the 200 firms surveyed in Quito and Guayaquil has been a generally positive one. Since their founding an average of 10 years ago, employment has risen by an average of 42 percent -- 49 percent in Quito and 34 percent in Guayaquil (Table 1). The increase has been greatest in food products (72 percent for the two cities combined), clothing (92.7 percent) and construction materials (72.6 percent), less in metal products (22.9 percent) and negative in wooden products (-13.1 percent). The latter decline was particularly marked in Guayaquil, though growth was virtually zero in Quito also. Overall, the employment figures demonstrate the employment creation

potential of small manufacturing in Ecuador, but they reveal a slower growth than has, under probably more favorable circumstances, been achieved in cases like Colombia during the 1970s. Our data on changes in sales, while less solid due to the need to deflate current prices values, refers to the important period 1980-1984. It shows considerable variation across from but on average a considerable growth.

Estimates of the share of firms in their industrial branch which had followed since 1980 (presumably the respondents were referring in their answers to their industry in their city or perhaps even only the part of the city with which they were most familiar) varied disconcertingly across the respondents; median figures by city and branch of manufacturing are shown in Table-3. Judging by these responses, failures had been most frequent in the wood products industry and least frequent among food products and metal products firms. If the true disappearance was say 15 percent over this 4 or 5 year period, i.e. say 3 percent a year it would not be particularly high by observed norms for small enterprise. But this is of course a very imprecise sort of estimate, as reflected by a high range of responses coming from firms in the same industrial branch (though it is true that within each of the broad categories we use here not all the firms belong to exactly the same industry). It is not, however, inconsistent with the entrepreneurs stated expectations for their own enterprises over the next 2-3 years. Only 2.5 percent indicated they might abandon the business, 8 percent said they expected things to get worse, another 15.5 percent said they did not know what would happen, 20.5 percent expected little change and 53.5 percent expected an improvement. (Table 4). That latter optimism was much more marked in Guayaquil (62 percent) than in Quito (45 percent).

In assessing the reasons for recent (since 1980) business failures among their competitors, the firms in our sample singled out the bad economic situation as the

most frequent cause (Table 9). The list bears a considerable resemblance, as one would expect, to the factors the respondents felt could help their own prospects. The major difference is in the greater prominence here of administration problems, which were cited more frequently than lack of credit; this may suggest greater realism and/or greater insight into the problems of other firms than of their own, and probably gives a fairly valid picture of events. Problems with raw materials and imports are mentioned again the infrequency with which labor problems are mentioned is worth nothing.

In spite of the still less than buoyant condition of the Ecuadorean economy, most of the sampled firms had plans to improve their operation; 59.2 percent of those answering this question planned to invest more in the business, 41.4 percent to put a new product on the market; on the other hand only 16.8 percent planned to increase the number of workers (Table 5).

A scattering of firms (10 percent overall) said that a decrease in bureaucratic obstacles would help them. Views on the priority steps to help raise sales vary somewhat by present of enterprise. More credit, in particular, is viewed as important by a much higher share of the smallest firms than of the largest (See Table 8). For the smallest firms, getting more credit seemed to be the issue and complaints about guaranties, etc. were rated; for larger firms the first consideration became more important and de second less so. Competition from imports on the other hand, was cited by 33 percent of firms with sales above 5 million sucres but only by 15 percent of those with sales below that level; assistance in exporting was cited by 20 percent of the former group but only by 11.8 percent of the larger group.

In the clothing and metal products industries, imports (legal or otherwise) were also cited by a considerable number of firms, 60 percent in the case of clothing (See Table 10). While there is extensive competition among small producers in all of these industries, large producers provide significant competition (being cited by 55-70 percent of respondents) in food products, furniture, and construction materials, but are cited by less than a third of the small producers in clothing and metal products. In these two, by contrast, imports provide a major source of competition.

**TABLE E-1**

Employment, by Worker Category, When Firms were Stated and Now, by Branch and by City

Employment	Food Products		Clothing		Wooden Furniture + Accessories		Construct. Materials		Metal Productos		All Sectors		TOTAL
	Quito	Guayaquil	Quito	Guayaquil	Quito	Guayaquil	Quito	Guayaquil	Quito	Guayaquil	Quito	Guayaquil	
<b>At Beginning:</b>													
Hired	7.05	9.40	10.10	4.85	11.15	13.00	10.04	6.95	14.10	11.70	10.65	9.18	9.92
Permanent	6.80	8.80	9.85	3.85	10.35	11.40	7.16	6.55	13.20	10.55	9.47	8.23	8.85
Temporary	.25	.25	.25	1.00	.80	1.60	3.68	140	.90	1.15	1.18	.95	1.07
Family	1.28	.40	.70	165	.45	1.0	.26	145	180	.65	.70	.63	.66
Total	8.33	9.80	10.80	5.50	11.60	14.00	11.10	7.40	14.90	12.35	11.35	9.81	10.58
<b>Now:</b>													
Hired	14.25	15.60	20.35	9.20	12.15	8.45	17.42	13.15	16.15	15.30	16.06	12.34	14.20
Permanent	13.0	14.75	20.0	6.45	10.40	7.20	9.84	11.50	15.25	14.60	13.69	10.90	12.30
Temporary	1.25	.85	.35	2.75	1.75	1.25	7.58	1.65	190	.70	2.37	1.44	1.90
Family	.81	.60	1.16	.80	.70	.95	.63	.55	1.05	1.00	0.87	0.78	0.82
Total	15.06	16.20	21.41	10.00	12.85	9.40	18.05	13.70	17.20	16.30	16.93	13.12	15.03

Source: Mission Survey of 200 small manufacturing firms in Quito and Guayaquil.

Note: Figures on Growth of Sales are not presented for all categories as rounding errors are likely to be too serious when the number of observations is low.

TABLE E-2

Average Annual Growth of Employment and Sales, by Age of Firm and by City

AGE OF FIRM	ALL	QUITO	GUAYAQUIL
1 Year			
Employment	106	114	78
Sales	6.5		
Number of Firms	9	6	3
2 Years			
Employment	23.1	25.8	21.3
Sales	11.1		
Number of Firms	18	8	10
3 Years			
Employment	12.5	11.0	14.5
Sales	32	39.0	15
Number of Firms	21	12	9
4 Years			
Employment	16.8	11.1	21.4
Sales	- 3.0	0.8	- 5.3
Number of Firms	18	7	11
5 Years			
Employment	2.0	3.1	- 1.0
Sales	8.0	18.5	- 16.3
Number of Firms	15	11	4
More than 5 Years			
Employment	n.a.	n.a.	n.a.
Sales	2.0 ±	- 0.6	4.1
Number of firms	119	56	63

Table E-3  
 Median Percent of Firms in their Industrial Branch which Respondents Believed to  
 Have Folded Since 1980, by City

Branch of Manufacturing	Quito	Guayaquil	Both
Food Products	10	15	10
Clothing	15	9	12
Wood Products (Mainly Furniture)	16	22	19
Construction Materials	15	12	14
Metal Products	8	11	10
All	13.0	14.5	13.8

Table E-4

Expectation of Entrepreneurs with Respect to the Future of their Business  
over the next 2 or 3 Years, by Branch and by City.

	Branch of Industry							
	Food Products	Clothing Products	Wood Products (Mainly Furniture)	Construct. Materials	Metal Products	All	Quito	Guayaquil
May Abandon the business	2.5	2.4	7.5	0	0	2.5	2.0	2.9
Business will worsen	7.5	12.2	2.5	10.5	7.3	8.0	8.2	7.8
Don't Know	17.5	22.0	5.0	13.2	19.5	15.5	22.4	8.8
Business will Remain about the Same	15.0	22.0	31.7	18.4	14.6	20.5	22.4	18.6
Business will Improve	57.5	41.5	51.2	57.9	56.5	53.5	44.9	61.8

Table E-5

Planned Changes

Percent of Firms Planning to:	Food Products	Clothing	Wood Products (Mainly Furniture)	Construct. Materials	Metal Products	All	Quito	Guayaquil
Invest More	59.0	48.7	61.5	77.1	48.7	59.2	52.1	66.3
Put a New Product on the Market	38.4	48.7	28.2	11.4	51.3	41.4	50.0	32.6
Increase Number of Workers	15.4	25.6	7.7	17.1	17.9	16.8	15.6	17.9
Firms	39	39	39	35	39	191	96	95

TABLE E-6

Factors Which Would Most Help the Firm to Increase Its Sales, by Branch of Industry and by City.

(Percent of Firms Cited Each Factor)

Guayaquil	Food Products	Clothing	Wood Products	Construct. Materials	Metal Products	All	Quito	
1. Better General Economic Situation	77.5	65.0	72.5	77.5	57.5	70.0	68.0	72.0
2. More Credit	60.0	60.0	60.0	60.0	57.5	59.5	56.0	63.0
3. Less Guarantees or Require- ments for Credit	15.0	35.0	12.5	10.0	22.5	19.0	21.0	17.0
4. Better Access to Inputs	50.0	27.5	50.0	32.5	47.5	41.5	33.0	50.0
5. Assist. on Promotion	32.5	10.0	20.0	30.0	25.0	26.5	35.0	18.0
6. Less Imports	10.0	45.0	5.0	17.5	32.5	21.0	25.0	17.0
7. Help in Export- ing.	7.5	17.5	20.0	12.5	15.0	14.5	20.0	9.0
8. Less Bureaucracy	5.0	12.5	10.0	10.0	15.0	10.0	11.0	9.0

Table E-7

Services Most Desired by Small Manufacturing Enterprises,  
by Branch and By City

(Percent Citing each Service)

Branch of Industry

	Food Products	Clothing Products	Wood Products	Construct. Materials	Metal Products	All	Quito	Guayaquil
Credit	65.0	52.5	80.0	72.5	65.0	63.5	57.0	70.0
Technical Assistance	37.5	72.5	30.0	32.5	47.5	41.0	41.0	41.0
Training	15.0	20.0	22.5	10.0	32.5	21.5	25.0	18.0
Marketing & Information	7.5	5.0	7.5	7.5	10.0	7.0	11.0	3.0
Control of Imports	12.5	7.5	7.5	5.0	2.5	7.0	9.0	5.0
Help in Exporting	2.5	7.5	0	2.5	2.5	4.5	7.0	2.0

Table E-8

Views on what would be most Helpfull in Increasing Sales, by level of Sales in 1984: Percent of Firms citing each Factor.

Factors Helpful in Raising Sales	Level of Sales (Millions of Suces)					
	Less than 1	1-5	5-10	10-20	Above 20	All
1. General Economic Situation	81.6	58.6	74.4	70.0	75.0	70.0
2. More Credit	71.4	61.4	53.8	50.0	37.5	60.5
3. Assistance on Promotion	42.9	45.7	43.6	35.0	50.0	41.5
4. Less bureaucratic Obstacles	6.1	21.4	2.6	5.0	0	10.0
5. Less Guaraneest Requirements to Get Credit	10.2	17.1	23.1	20.0	6.3	19.0
6. Eetter Access to Inputs	42.9	45.7	43.6	35.0	50.0	41.5
7. Less Inputs	16.3	14.3	26.2	40.0	37.5	21.0
8. Help in Exporting	10.2	12.9	20.5	20.0	18.8	14.5
Number of Firms	49	70	39	20	16	7 194

Table E-9

Reasons Given by Respondents for Business Failures Among their Competitors  
Since 1980, by Industry: Percent of Firms Citing Each Reason.

Reasons for Failure of Competitors	<u>Branch of Industry</u>							
	Food Products	Clothing	Wood Products (Especially Furniture)	Construct. Materials	Metal Products	All	Quito	Guayaquil
Bad Condi- tion of the Economy	22.5	30.0	22.5	22.5	20.0	23.5	27.0	20.0
Weak Adminitra- tion of the Firm	10.0	25.0	25.0	27.5	12.5	19.5	24.0	15.0
Lack of Credit	12.5	17.5	17.5	27.5	10.0	17.0	16.0	18.0
Lack of Raw Materials	5.0	10.0	10.0	15.0	7.5	9.5	10.0	9.0
Competition from Im- ports (Legal or Contraband)	5.0	17.5	0	2.5	7.5	6.5	12.0	1.0
Labor Problems	2.5	10.0	2.5	2.5	0	3.5	4.0	3.0
Other	2.5	7.5	12.5	7.5	2.5	6.5	5.0	8.0

Source: Mission Survey

TABLE E-10

Main Sources of Competition for the Sampled Firms in Quito and Guayaquil, by  
Industrial Branch  
(Percent citing each source)

Main Sources of Competition	Food Products	Clothing	Wood Products (Mainly Furnit.)	Construct. Materials	Metal Prod.	All	Quito	Guayaquil
Other Small Producers	67.5	72.5	80.0	87.5	67.5	75.5	70.0	81.0
Large Producers	60.0	27.5	70.0	55.0	32.5	50.0	48.0	52.0
Imports (Including Contraband)	7.5	60.0	5.0	12.5	35.0	23.5	24.0	23.0
No competition for some or all of products	12.5	2.5	10.0	7.5	5.0	8.0	12.0	4.0

Note: Figures are downward biased and perhaps otherwise distorted since some firms did not respond to the question.

TABLE E-11

For Entrepreneurs Awareness of and Benefits Received From Various Institutions, by Branch and By City 1985

	Food Products		Clothing		Wool Products (Mainly Furniture)		Construct. Materials		Metal Products		All		Quito		Guayaquil	
	Aware	Benefits	Aw.	Ben.	Aware	Benefits	Aware	Benef.	Aware	Benefits	Aware	Ben.	Aw.	Ben.	Aware	Benef.
MICEI	90	40	70	22.5	80	22.5	77.5	17.5	77.5	25	75	25	78	22	72	28
CENAPIA	70	5	70	7.5	50	7.5	62.5	5	65	10	63.5	7	66	4	61	10
SACAP	87.5	15	90	17.5	82.5	22.5	85	15	90	25	87	19	85	15	89	23
CENDES	67.5	7.5	57.5	0	47.5	5.0	55	10	72.5	7.5	60	6	68	7	52	5
FOFINAR	65	15	52.5	17.5	55	17.5	55	15	55	7.5	56.5	14.5	66	17	47	12
INFI	60	5	47.5	0	30	0	52.5	7.5	70	12.5	57.5	5	64	6	39	4
CENCA	22.5	2.5	12.5	0	12.5	0	12.5	0	15	0	15	0.5	18	0	12	1
FOPEX	32.5	0	32.5	0	25	0	35	0	35	0	32	0	38	0	26	0
OCFPA	67.5	2.5	55	0	65	0	55	0	55	0	59.5	0.5	70	0	49	1

TABLE E-12

Entrepreneur's Views on Which of Four Institutions Provides the Most Support to the Firm, by Branch and by City  
(Percent putting each Institution First)

Institutions	Food Products	Clothing	Wooden Products (Mainly Furniture)	Construct. Materials	Metal Products	All	Quito	Guay.
MICEI	20	15	10	10	17.5	14.5	12	17
CENAPIA	2.5	12.5	10	5	2.5	6.5	4	9
FENAPI	12.5	15	15	20	17.5	16	21	11
SECAP	0	10	10	7.5	10	7.5	5	10
MORE OF THE ABOVE	65	47.5	55	57.5	52.5	55.5	58	53

TABLE E-13

DISTRIBUTION OF FIRMS BY HOW THEY WOULD CHANGE THE LEVELS OF INPUTS WERE SALES TO INCREASE SUBSTANTIALLY: FIRMS CLASSIFIED BY LEVELS OF EMPLOYMENT.

	NUMBER OF WORKERS									
	1-2	3-5	6-10	11-15	16-20	21-30	/31	1-15	/16	All
Hire More <sup>a</sup> Permanent workers	58.3	42.4	42.4	55.5	37.0	45.0	35.3	46.6	39.0	44.1
Hire More <sup>a</sup> Temporary workers	0	18.2	10.2	0	18.5	15.0	11.8	9.2	15.6	11.3
Increase Use of <sup>a</sup> Overtime	16.7	21.2	25.4	11.1	37.0	20.0	29.4	20.6	29.7	23.1
Increase Work Force in useful ways	8.3	0	1.7	3.7	0	5.0	5.9	2.3	3.1	2.6
Subcontract Part <sup>a</sup> of work to other Firms	0	17.1	15.3	22.2	0	5.0	11.8	14.5	4.7	11.3
Invest in More Machinery	8.3	3.0	3.4	7.4	7.4	5.0	5.9	4.6	6.2	5.2
Do Nothing	8.3	3.0	1.7	0	0	0	0	2.3	0	1.5
Other	0	0	0	0	0	5.0	0	0	1.6	0.5
Number of Firms	12	33	59	27	27	20	17	131	64	195

a) Responses specified in the questionnaire. Other responses were spontaneous.

ANNEX F

NOTES ON FREQUENCIES AND CROSS-TABLULATIONS RELATING TO  
INSTITUTIONAL KNOWLEDGE OF ENTREPRENEURS AND THEIR VIEWS WITH RESPECT  
TO SUPPORT RECEIVED FROM INSTITUTIONS

MICEI ranks first among small-industry-related institutions from which sampled entrepreneurs report having received benefits: 25 percent of the surveyed firms indicated that they had obtained benefits from MICEI, with no significant regional differences. SECAP and FOPINAR rank second and third respectively in the list of institutions from which firms have received benefits with 19 percent and 14.5 percent respectively .

Our tabulations also show a rather widespread ignorance among producers regarding the functions of institutions concerned with small industry. Thus, the percentages of all firms sampled that were unaware of the various institutions (with a relatively larger degree of ignorance in Guayaquil), were: 36.5 percent for CENAPIA, 40 percent for CENDES, 43.5 for FOPINAR, 40.5 percent for OCEPA, 48.5 percent for INEN, and well above 50 percent for CEBCA and FOPEX.

The importance of MICEI in terms of the awareness and benefits received by entrepreneurs is somewhat confirmed by tabulations for question 6.10. True, when asked "which Institution among MICEI, CENAPIA, FENAPI, AND SECAP, provides the greatest support to your enterprise", more than half of the entrepreneurs chose "none"; but of those who did answer positively , 32.5 percent selected MICEI. Interestingly, a slightly higher percentage (35.9 percent) stated that FOPINAR was

the institution that provided the most assistance to their enterprise (even though it did not appear explicitly in the list of institutions mentioned to the respondents), with a strong regional difference in the answer: 50 percent of Quiteño entrepreneurs who answered positively to 6.10, selected FOPINAR, while in Guayaquil the corresponding percentage was only 23.4 percent.

Cross tabulations between age of the firm (1.4) and perception of institutional support (6.10) indicate that the two variables are essentially independent. Neither knowledge of the functions of MICEI nor "classification with MICEI" are sufficient conditions for a firm's receiving benefits from MICEI, according to our sample. In fact, while 47.5 percent of all sampled firms are "classified with MICEI" (question 6.6) only 25 percent indicate that they had received benefits from it.

All in all, analysis of tabulations concerning knowledge of and/or support from institutions reveal the existence of two rather independent types of problems: (a) an informational void that apparently prevents entrepreneurs from knowing something as basic as the functions of certain institutions, and (b) difficulties and delays in cutting through the "red-tape".

## FREQUENCIES & CROSS TABULATIONS RELATING TO EMPLOYMENT

More than 46 percent of the entrepreneurs interviewed would prefer not to expand the number of permanent jobs in the firm if their sales were to grow. This group would prefer to create temporary jobs, increase overtime, or subcontract. There seems to be a regional difference among those who prefer to increase overtime with Guayaquileño entrepreneurs exhibiting a greater propensity to expand overtime than quiteños (19 percent against 6 percent, respectively).

Those entrepreneurs who expressed their desire not to hire permanent or temporary workers if their sales were to rise, pointed to the following main reasons: the high level of the minimum wage (47.2 percent), problems with the quality of the workforce (21.3 percent), and the fear of the formation of a "Comité de Empresa" (16.8 percent). Problems with the quality of labor (qualifications, skills, etc.) was offered spontaneously by interviewed entrepreneurs as a reason for not hiring more permanent or temporary workers; this answer was not explicitly listed in the questionnaire. Interestingly, the fear of a "Comité de Empresa" appears to be more pronounced among Quiteño entrepreneurs than among Guayaquileños. Manufacturing sector or age of the firm made no significant difference in the frequency distribution of answers; entrepreneurs' perceptions regarding minimum wage legislation, "Comité de Empresa" and the quality of the work force as barriers to job creation cut across sectors and affect young as well as old enterprises.

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The cross-tabulation between question 4.7 (whether and in what manner employment would be expanded should sales increase) and question 4.1 (total number of workers presently employed) reveals that the willingness to increase permanent jobs is greater among enterprises having a total between 6 and 15 of workers, 45.9 percent of such entrepreneurs indicated that they would hire more permanent workers should

their sales increase, currently operate with a total number of workers ranging from 6 to 15.

This result, however, is biased by the nature of or sample, for 43.5 percent of all the enterprises surveyed have current levels of total jobs in the 6-15 range.

Subcontracting is not a very widespread practice among the establishments in our sample: only 18.5 percent of the surveyed firms subcontracted for more than 20 percent of the value of their sales; there are no significant differences in the extent of subcontracting among sectors or between the two cities.

Comparison between the frequencies for question 4.5 (whether a "Comité de Empresa exists or not) and question 4.1 (total number of workers currently employed) yields an interesting insight into the practical irrelevance of the labor code in the small-industry sector. Close to 33 percent of all surveyed firms currently employ over 16 workers (permanent plus temporary). Nevertheless, 96 percent of all interviewed entrepreneurs reported that their companies have no "Comité de Empresa". This result is the more striking considering that there could have been an incentive for the entrepreneur to conceal the truth and say that a "Comité de Empresa" exists in his/her firm when in fact it does not. Our sample rules out the possibility that the widespread absence of a "Comité de Empresa" among surveyed firms could be explained by a large number of unpaid or family workers in the firms. The average number of unpaid and family workers currently employed in the enterprises samples' is only 0.86 in Quito and even less in Guayaquil. Neither sector nor region nor age of the firm introduce significant differences in the lack of "Comité de Empresas" for firms with more than 15 employees --the phenomenon is widespread.

Cross tabulations between questions 4.1 (total number of workers now) and 1.4 (age

of the enterprise) show no significant covariance. This suggests that a substantial degree of fluidity and large fluctuations in employment levels may characterize the small-industry sector. Thus, while most firms sampled (74 percent) employed between 3 and 20 workers, this employment pattern is basically the same for young as well as older firms, i.e., older enterprises do not necessarily have more workers than to young ones. These results could alternatively suggest that there is a certain ceiling beyond which employment in small-firms tends not to grow, with the implication that older firms would not show significant employment differences than young ones. But the main explanation is that faster growing firms exist from the size range under discussion and hence do not enter our sample.

In terms of rates of growth of total employment between the time when a firm was established and the time of survey, our sample exhibits a slightly greater percentage of enterprises experiencing increases in labor employment than decreases or stability. Nevertheless a significant minority of 36.5 percent of sampled firms reported negative or zero annual rates of increase in total employment. In both Quito and Guayaquil, the sectors whose firms most frequently experienced employment contraction were "wood products" and "metal products, machinery and electrical equipment", where 52.5 percent and 50 percent, respectively, suffered declines. So, while region (Guayaquil vs. Quito) seems to make no difference in the employment trends of surveyed firms, sector does make a difference.

It is interesting that the sector "construction materials" ("Non-Metallic Minerals") did not rank high in employment reduction, in spite of the fact that in recent years Ecuador has been characterized by a construction "slump" relative to the late 1970s. Age of firm cannot account for this result, since our sample shows an almost even split between young (5 years or less) and old (6 or more years) firms in the "Construction Materials" sector.

The search for possible determinants of employment growth yields some strange results which might reflect more the characteristics of our sample than of the universe of firms in this sector. For example: of all the quiteño enterprises that exhibited an annual rate of increase in employment of 11 to 20 percent, 86 percent are firms that have been in operation for 5 or more years; in contrast, guayaquileño enterprises with rates of employment growth in the same range include both young and old firms. Nevertheless, there is evidence to support an expected result, namely, that younger firms expand employment at higher percentage rates than do older ones, due to the simple mathematics of percent growth; in fact, 78 percent of all those sampled firms exhibiting annual rates of employment creation of 21 percent or more have been in existence for 4 years or less; likewise, 92.6 percent of firms with annual rates of employment increase ranging from 1 to 10 percent were established 5 or more years prior to the survey date.

## FREQUENCIES AND CROSS TABULATIONS REWAKING TO CREDIT

When entrepreneurs were asked which three services they would like to receive in order to improve the business, 38.8 percent of all valid answers (i. e. excluding errors and blanks) cited credit-related services, including more availability of credit and simpler application procedures. This frequency distribution is essentially independent of sector and region.

Similarly when the entrepreneurs were asked what would allow them to increase sales (3.11), "greater availability of credit" ranked second as the most frequent answer. (after "a better overall economic situation") constituting 21.4 percent of all answers. Again, regional and sectoral differences were not significant.

A rather significant share of the 200 enterprises sampled in Quito and Guayaquil (28 percent) had not received credit in the last two years (question 2.3). This seems to be strongly linked with the age of the firm, as 59.6 percent of all those who had not received credit had been operating for more than 6 years at the time of the survey. This might be explained by either or a combination of the following hypotheses: (a) older firms tend to be owned or managed by older entrepreneurs who are, perhaps, more traditional in their business practices and tend to have less skill and willingness to go through the somewhat complicated steps required to obtain credit in the formal financial system; (b) firms that have survived 6 years or more are more likely to have solved their financial difficulties and more apt to maintain and/or expand their operation out of retained earnings. Unfortunately, our sample data on age of the entrepreneur is not detailed enough to throw light on the first hypothesis. While it is true that 63.3 percent of entrepreneurs 30 years of age or older are in charge of firms established 6 or more years ago, and that 91 percent of entrepreneurs who had not received credit in the last two years are 30 or

more years old, it is not valid to include entrepreneurs in the thirties in the group of "traditional-old" managers unfamiliar with and unable to deal with credit-application procedures. Only 18.5 percent of the entrepreneurs interviewed are 50 years of age or older. In contrast, 65.5 percent of entrepreneurs are between 30 and 50 years old; how many of those included in this category are lacking the education and/or "modern" cultural traits to deal with formal credit systems is impossible to ascertain on the basis of our data.

Women -although accounting for only 20 percent of the sampled entrepreneurs- seem to be slightly discriminated against by the credit system. In fact, 38.5 percent of all female entrepreneurs interviewed had not received credit in the two years prior to the survey date, while this was true of only 26.9 percent of male entrepreneurs interviewed. Of course, an alternative hypothesis is possible, i. e., that women are more efficient entrepreneurs and are better able to maintain and expand the firm out of retained earnings.

About 29 percent of the surveyed entrepreneurs had not received credit in the two years prior to the survey. Another 17 percent had received credit only from money-lenders. This is, indeed, not a very large proportion. It suggests that the situation for small industrialists in Ecuador, as far as credit is concerned, is not characterized by a great deal of borrowing in informal credit markets. In fact, 76.5 percent of those receiving credit in the past two years had recourse to the formal financial system (i. e., commercial banks, the Banco Nacional de Fomento, and Savings and Loans Associations). Interestingly, a larger proportion of Guayaquileño entrepreneurs (34 percent) received credit from private money-lenders as compared to Quiteños (19 percent).

As might be expected, access to formal credit systems is visibly linked to the

legal-organizational status of the firm. Thus, over 68 percent of all those enterprises which did not receive credit are "sole proprietorships" (sociedad unipersonal)-without significant regional differences. Similarly, if we lump those firms which have not received credit with those who received credit only from private money-lenders, it can be seen that most of them (54.4 percent) are sole proprietorships. By contrast, out of all enterprises whose legal status is that of a "limited-responsability company" or of a "corporation", 61.5 percent received credit from the formal financial system. These results, however, must be interpreted with some care, given that our sample is heavily weighted toward sole proprietorships 49.5 percent of all sampled enterprises have this legal status.

Neither having received credit nor the particular source of credit seems to be correlated with rates of growth in employment. Perhaps firms with access to credit prefer to substitute capital for labor when possible.