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MICRO AND SMEs DEVELOPMENT IN RURAL AREAS IN LATIN AMERICA:

**Preliminary notes on lessons from theory and practice for the Transition of rural
enterprises from refuge goods to higher value products and more dynamic
markets**

by

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Introduction

There is very little systematic information about micro and SMEs and the criteria for their definition vary not only from country to country (table 1) but also from one public organization to another. In very rough terms it is possible to say that micro, small and medium enterprises represent between 95% and 99% of the number of manufacturing enterprises in Latin America, they employ between 60% and 90% of its labor force and produce between 25% and 40% of their output (table2). In 9 out of 10 countries for which there was information productivity increased but only in four of them the employment did the same ; only in one country both, employment and productivity decreased (table 3) In most counties, less than 40% of SMEs are agro related and the majority of them, with few exceptions are in the food production segment (Table 4)

The regional economies have experienced radical changes in rules of the game for the operation of rural development projects. Structural adjustment, privatization, trade and financial liberalization have had very asymmetric impacts in the rural areas benefiting some products, some regions and some producers normally medium and large in rain fed areas Due to liberalization and improvements in rural infrastructure rural firms, once protected by distance or policies are put into direct competition with foreign and urban firms, “pouring cheap manufactures into rural areas and into towns and cities where “exports” from the rural areas will have to compete”

To face the new demands, agglomeration theories, cluster development theories and those explaining the development of new industrial districts have become frequent references in the current debate on industrialization in Latin America but with little reference to rural development. Of all the different sources, it has been the experience of the North- Central f Italy the one that has generated most of the enthusiasm, particularly among “agraristas” because it was based on the incorporation of small farmers in the production of highly competitive products for the world market taking advantage of the flexibility that family labor was able to provide

What are the lessons for rural development from those areas that were able to compete under the new conditions of the world economy?

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Announced in a nutshell we think that were built on two interdependent pillars : on changes in the patterns of production and on the development of enabling institutions as systems of networks and alliances. As regards the first pillar, it consisted of the dissemination of knowledge, the introduction of technical innovations; the diversification of output in products that did not depend on “big science” (in small local economies) and in serving dynamic markets,

2, Technical Innovations: product, process and management

Product Innovation cases:

Pineapple vinegar in Honduras: The outreach activities of the Zamorano School in Honduras through his PROEMPRESAH /BID program assisted in the formation of an Empresa Asociativa of pineapple producers with 274 members; 10 of them, introduced a low cost process for the production of an organic pineapple vinegar (using artisan filters of stone and ceramics) of a highly acceptable quality for the supermarkets that competes with artificial and imported vinegars. A similar experience is the one of ACOPROSAVI El Salvador where a group of 36 partners (4 of them women) went into transformation of fresh chilies into Tabasco sauce through maquila agreements for export and import substitution

Specialty cheese in Ecuador, Peru and México: Queserías Rurales of Las Salinas in Ecuador where a coop that had a long tradition in the production of traditional fresh cheeses changed to the production of a variety of specialty cheeses as a result of technical assistance received from the Swiss. Its well known products are distributed through the coops own shops and through the supermarkets. Beyond that they have become a school of cheese making for other peasant communities. A very similar experience can be found in Arequipa Peru with the Coop La Campina and as a project in process of development in Ocosingo Mexico where the idea is to upgrade a traditional cheese to become a certified original product with all the technical, legal and marketing implications

Process Innovation cases

Cashew Nuts in Brazil : Cashew is the main crop in Serra do Mel, Rio Grande do Norte and provides a large part of the income of the rural population. Before the project, beneficiaries sold cashew *in natura* to a cooperative created with assistance from a government program. The cooperative processed the cashew with a large-scale technology, classified, and packaged it. Through the initiative of a government extensionist a new project introduced small-scale technology that could be used by individual farmers that had a low cost, produced a significant reduction of broken nuts (from 20% to 5%) and improvement in quality due to family processing. In addition, they learned to carry out a first classification before sending the nuts to a newly created cooperative since the old one opposed the introduction of the new technology. As a result of the project, farmers have substantially increased their revenues from US\$1.66 per kilogram to US\$4.80/kg.

Organic Coffee in Bolivia, México and Guatemala There are several examples of process changes in the area of coffee from the traditional kind to organic and specialty coffees. The case of Alimentos naturales de Irupana in Bolivia began in 1988 through the initiative of an ex ONG director, frustrated with the corrosive effect of donations and taking advantage of his former relation with peasant communities initiated a food business in order to give their products an industrial and market destiny comparable to other more modern consumption goods of upper and middle classes. Arrangements were made with peasants from different ecological strata to change to organic coffee and also to produce with organic techniques honey and other bees products and a list of vernacular products (amaranto, coca leaves, peanuts, quinua, cañahua, tarhui etc.) The "Mexico project" is in the Chiapas region, and was started by the Catholic Church and supported by them and the Mexican government. The large cooperative (ISMAM) produces processes and markets organic coffee in national urban centers and in Europe. It started in 1985, comprises 196 rural communities and groups, with over 1500 members and has registered 'Café Mam' as a gourmet mountain coffee. ISMAM has also its own laboratory in charge of the production of inputs for the biological control of pests.

A similar experience is that of the Sierra de los Cuchumatanes Project in Guatemala that introduced changes on traditional practices in order to obtain organic coffee certificate and begin to open new export venues with one of the Fair Trade kind of international organizations

Management Innovation cases

Wine in Chile Vinos Lautaro is an association of 16 small grape producers in the Central Valley that were used to sell its wine in bulk but, after visiting other experiences in Argentina and receiving technical and administrative assistance from a state agency, they had to introduce important changes in current practices: in the quality of the water used; in the sanitary conditions of their warehouses, baths and other installations; in the establishment of recording system of pesticides and fertilizers; in the management of compost; in the trazability of inputs, etc after this changes they were able to produce state bottled wines for the internal market and for export to Belgium, Germany Sweden and Denmark.

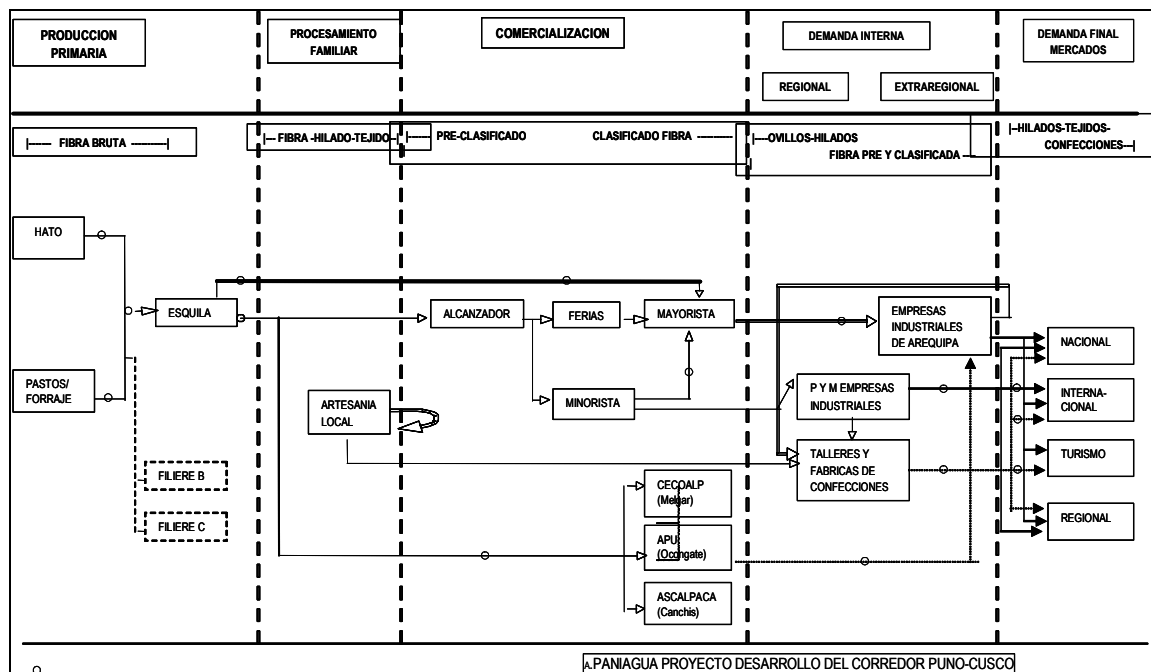
Wood artisans in Argentina The wichis artisans (an indigenous people of the northern provinces) used to sell their wood works in the internal market for more than 20 years to tourists and to nationals. The country economic crisis reduced drastically the purchases by Argentineans so that the need to export became an urgent necessity. In order to achieve that, a catalog of more than 300 different designs was produced and exports began to grow; to further this trend, an arrangement was made with an Internet page linked to some Free Trade kind of organizations as a means to sell both at retail and wholesale levels, there is a strong possibility that sales will grow even faster than in the last two years given the devaluation of the peso

A conclusion related with the need for introducing innovations would indicate that in an open economy peasant business firms cannot improve on regular market exchanges when trading undifferentiated commodities on the spot or on wholesale markets. In fact, firms involved in non traditional products and in markets with high transaction costs can have had more of an economic impact on their member

3. The systemic nature of successful experiences

We usually perceive a successful enterprise as an isolated phenomenon when, in fact what we are seeing is only, so to say, the tip of the iceberg, because competence is of a systemic nature where the successful enterprise is the visible part of a network of direct and indirect relations with other agents providing inputs, services, knowledge, information etc. In all of the cases a crucial part of the projects' success in linking to the identified demand is a careful attention to the various links of the product chains because initial success at one level of the chain can be undermined by bottlenecks at other levels.

Explicit bottlenecks in the the alpaca chain in Puno Peru



The circles represent bottlenecks that the project is supposed to overcome with a significant impact on income and productivity for most of the participants in the chain

Tomatoes production in Petronila Juaceiro Brazil In contrast to most rural development policies which separate interventions focused on small farmers from those on large capitalist enterprises, the federal government, using its heavy investments in irrigation as the incentive to induce large firms to participate in this approach. gave to the company in charge of the irrigation projects (CODEVASF) the responsibility of inducing contracts between large firms and established small farmers, for providing them with technical assistance; it also arranged with a Regional Bank to provide small farmers with credit for working capital under the condition that they cultivate tomato for processing and made an agreement with the Agricultural Research Institute to concentrate efforts on the production of varieties of tomato for processing. Finally, it transferred the administration of each project to an institution comprising representatives of small farmers and large firms. In order to ensure a good relationship between them and to monitor the good administration of the projects CODEVASF was accepted as mediator by both parties.

Chrysalides in Costa Rica The project contributed to change the practice of an embryonic organization of women from the production of artisan works with butterfly wings to be sold to tourists. to the production of chrysalides for export. A course on the biology of butterflies and on their feeding needs was delivered to the group by a experimented biologist including a the recognition of the different varieties and on their scientific names together with visits to other butterfly breeders, the purchase of new specific inputs for packaging and delivering. As a result of all this, they have been increasing the number of chrysalides for export, hoping to reach 4000 per month in the high season (US\$ 5000)

4. External demand as a driving force

In contrast with what is usually emphasized in some of the rural development and poverty literature when dealing with participation, it is the external demand for the actual or potential products and resources of the rural families that is the critical element to consider and guide the demands of them and not the other way round. as some of the successful examples presented clearly show. On the other hand, using demand as the point of departure in project design for changing production patterns is critical to avoid the costs of frequent mistakes that tend to promote activities based on the existence of a given technology for the available and known resources. (“we used to try to sell what we produced and not to produce what could be sold”)

Two contrasting experiences

The avocado oil production in Michoacán illustrates the problems of not putting demand at the outset in an apparently sound project. A manufacturer of essential oils for the cosmetic industry taking advantage of a state program that promoted associations of enterprises with ejido peasants financing the investment and current costs with the peasants as co debtors . the technology was there and abundant avocados were there but market only for less than 20% of what was produced so that the peasants were left with the debt and rotting 17 tons of oil

This experience contrasts with that of Sadia, from Brazil one of the largest producers and exporters of broilers in the world that organized a complex contractual procurement system involving in its high around 4000 peasant families in charge of fattening broilers and of cultivating part of the corn used in the feed. The company has an established procedure for selecting the families (“we don’t work with absentee owners because peones lack interest in being careful”) and they assist in designing the project, they guarantee the loans to the bank, provide all the inputs and buys the whole output. This arrangement seems to have made Sadia more competitive than other vertically integrated large enterprises in the field.

5. Institutional development

The second pillar for the transition from refuge enterprises to higher value products for more dynamic markets is the development of enabling institutional arrangements between the direct and indirect stakeholders of the initiative. This was the case in all the successful cases described and is also illustrated by the contrasts between the experience of the following cases.

IRUPANA’s institutional obstacles In Bolivia, any productive initiative, no matter how small, as soon as it needs more than one horse power of electric energy has to go through a maze of permits and regulations to obtain its legal status, the tax payer identity card, ten municipal licenses, the approved groundplot etc. Therefore any formal small enterprise begins to pay taxes even before they have earned a single peso. The first obstacle is the value added tax that does not take into account that most of your costs are the inputs bought from peasant producers that for obvious reasons cannot collect or pay VAT so that your cost is 15% higher than that for those whose inputs are from formal providers. The second obstacle is the municipal licenses and patents that you have to renovate every year and for them you pay the hygiene inspection fee and the garbage collection tax that you already paid it in your residence tax and in fact for the private collector because the public service is a virtual one. Another municipal tax is the one for the publicity sign in front of your shop. But here your worries don’t end, since you deal with food, you have to pay for the bromathological analysis but there is a dispute between three authorities as to who is responsible so that you receive inspectors from the three. None of them is interested with your compliance and in every procedure you have to bribe lesser bureaucrats that are regular visitors to check your various licenses

“When we finally were able to buy a plot in the industrial zone of Villa Fátima which was only two blocks from the main avenue, we had to pay for 70 mts of electric cable, the meter and the transformer that are supposed to be provided by the electric company and also for the external connections to the water and sewer facilities. The Municipality was not even able to fill the holes made for all this installations”.

Enabling institutions in some districts in Brazil This experience is in clear contrast with the three of the more successful Northern Brazil cases studied by Damiani for the WB (The cashew production in Serra do Mel, the tomato production in Petrolina-Juazeiro and garment making in Pernambuco) which are examples of the development of enabling institutional arrangements. In all of them, an alliance between state or municipal governments, large and small producers, research and or extension agencies and NGOs were able to “co-produce” (to use Orstom’s concept) the conditions for the sustainable development of small rural enterprises, contradicting the extended prejudice that NGOs can not or even should not work with government agencies and that associations between small and large producers are always exploitative of the former

Nevertheless, even in situations where public structures act as obstacles to small enterprise development, social capital as alliances between private agents can lead to successful results as shown the experience of the La Campana Society in the same country as IRUPANA (Bolivia) In the Ichilo province in Santa Cruz Bolivia, 532 families of the Antofagsta Colony began to cultivate rice after the crisis of sweeden agriculture in the tropical low lands, selling it through host of intermediaries with little control on the prices and classification criteria since those intermediaries themselves depended on a small number of mills. In this context, a NGO promoted the organization of the small rice producers in a so called Union of Labor Communities and, after its organization was established the NGO was able to persuade a large rice producer in the same municipality, form a society for the installation of a mill whose scale would be justified by the sum of the peasants and the landowner’s output. The NGO would contribute with 36% of the initial investment, the Union 14% and the rest by the landowner. So La Campana Society was formed and it was established that 90% of the NGOs participation would be transferred to the Union with the capitalization of the earnings leaving her with 10% to act as mediator

6. Territorial development as a social construct:

Most of the success cases mentioned are micro experiences, very often characterized by highly idiosyncratic elements that explain their success and seem to exist like islands in an otherwise sea of indifference or worst, of frustrated experiences, therefore it is appropriate to explore the kind of framework or approach that could help to project or up scale this successful experiences.

It seems intuitively logic to think of the space where this experiences are located, as the more immediate element that influences and is influenced by them, but not as a physical container but as a complex structure of interaction between heterogeneous agents and a physical environment in continual transformation: a territory. What we are interested in is on the kind of institutional architecture that will enable the changing of the production patterns with social equity and

sustainability of that territory. Without going into how to define the limits or boundaries of this rural territory and thinking on some instrumental implications for policy design,, it seems also logic to take some politico-administrative division as the point of departure that in the case of Latin America it could be the municipality and its Local Development plans as building block of a process of integrating micro (community?) experiences in a larger framework as some of the following cases tend to suggest.

The canton (municipality) Guamote in Ecuador

Until very recently Guamote was characterized by a series of haphazard initiatives from the Municipal authorities and a host of NGOs, each acting on their own in a clientelistic way. The municipal government was traditionally in the hands of mestizo families in spite of an indigenous people representing more than 90% of the population and most of the investments went to the urban nucleus. It is only in 1992 that an indigenous leader was able to gain the control of the town council and began the development of a highly idiosyncratic structure oriented to a participative elaboration of a Local Development Plan. (PDL). It included an Indigenous Parliament in charge of mobilizing the participation of the 117 communities of Guamote and of monitoring the compliance with the plan; a Local Development Committee in charge of coordinating the implementation of the PDL; a Municipal Council which is the institution legally authorized for assigning the budget.. In this context, the PDL has become the legitimating instrument for all the different investment or project initiatives and as a framework for negotiations between the interests of the different groups.

Three municipalities in North eastern Brazil

The Rural development policy in Brazil (in particular the PRONAF program) has established, as a condition for receiving program funds, the preparation of Municipal Rural Development Plans and the formation of Local Development Councils as the framework for reaching agreements between different actors. The way in which this condition is being implemented depends on the strength of the local civil society and on the political inclinations of the authorities. In Tombos a left wing prefecto allowed the development and participation of grass roots organizations in the formulation of the PMDR but after losing the next term election the process lost the backing of the new prefecto but continued as a mobilizing instrument for the grass roots organizations as a negotiating element for discussions with the authorities. In Araponga, where the political conditions for small agricultural producers were not very helpful, some NGOs began to develop organizational initiatives with the peasant communities around the preparation of a PMDR but not related with the electoral disputes, creating the condition for the traditional elite to associate herself in the preparation of the PMDR. The third municipio is in the hands of PT but the

grass roots movement is very weak and in contrast with the other two, the task assumed by some ONGs here is to initiate a grass roots mobilization in order to be able to develop a participative PMDR.

The transformation of San Joao municipal district

An illustrative case of the territory as a social construct is the experience of Sao Joao de Aruaru , a process induced by public procurement of wood works and furniture by the federal government that led to a development of an industrial cluster and to the strengthening of the identity of the municipality. "The Association of Furniture Makers ...had started with only four firms and had grown five years later to 42 (and) become a major civic institution in the town. Among other activities, it formed a permanent committee for the group purchase of timber...organized sharing of equipment...shared information about the purchase of secondhand equipment ...backward and forward links with firms in other sectors emerged...the sawmills...moved backward into. then assembly of sawmill equipment, and then equipment for sugarcane and cassava mills operating in the region, as well as for local manufacturers of cheese. Five storeowners bought trucks to transport timber from the forest. A new supplier of Amazonian hardwood set up business in the town. The bank of Brazil opened a new branch ... The flurry of new manufacturing activity and employment led to a spurt of housing construction. A new brick making operation opened up...and townspeople proudly showed visitors the old mud structures (to see) how their lives had improved .. (Tendler)

TABLES

Table 1
Classification Criteria

PAIS	MICRO	SME	LARGE	PYMES
Argentina	< 6			7 a 100
Bolivia	<5	5 a 15	15 a 50	5 a 50
Brasil	<20	20 a 99	100 a 499	20 a 499
Chile	<10	10 a 49	50 a 199	10 a 199
Colombia	>10	10 a 49	50 a 199	10 a 199
Costa Rica	>30			31 a 100
Ecuador	<10	10 a 49	50 a 100	30 a 100
México	<16	16 a 100	101 a 250	16 a 250
Nicaragua	<4			4 a 30
Paraguay	<6	6 a 20	21 a 100	6 a 100
Perú	<10	11 a 20	21 a 200	11 a 200
Uruguay	<5			5 a 99
Venezuela	<5	5 a 20	20 a 100	5 a 100

Table 2

Number, employment and output of manufacturing enterprises

	NUMBER			EMPLOYMENT			PRODUCTION		
	MICRO	SME	LARGE	MICRO	SME	LARGE	MICRO	SME	LARGE
Argentina	70,6	27,7	1,7	13,7	44,2	42,1	5,2	35,9	59,0
Brasil	86,3	13,0	0,8	16,4	42,8	40,7	7,8	34,8	57,3
Chile	82,1	17,0	0,9	39,2	48,2	12,6	4,4	23,7	71,9
Colombia	91,5	5,0	3,5	32,0	30,0	38,0	6,0	31,5	62,5
Costa rica	87,1	7,3	5,6	49,8	6,6	43,6	21,7	9,9	68,4
México	91,3	7,6	1,1	17,4	33,0	49,6	9,1	28,6	62,3
Nicaragua	89,5	9,2	1,3	21,5	9,8	68,7	9,5	10,3	80,2
Perú	67,4	31,7	0,9	26,1	51,5	22,4	13,7	46,2	40,1
Uruguay	66,4	32,3	1,3	12,1	52,2	35,6	0,0	39,7	60,3

Table 3
SMEs in Agriculture

Countries	Agro based SMEs		
	Agriculture	Other	Total
Argentina	16,1	11,2	27,3
Brazil	17,0	7,9	24,9
Mexico	16,4	9,7	26,1
Chile	22,1	15,6	37,7
Collmbia	19,9	7,8	27,7
Peru	20,0	7,3	27,3
Venezuela	19,1	7,9	27,0
Costa Rica	32,2	19,1	51,3
Nicaragua	25,9	16,0	41,9
Uruguay	30,6	8,9	39,5

Table 4
SMEs trends in employment and productivity

PRODUCTIVITY	EMPLOYMENT	
	INCREASING	DECREASING
INCREASING	Chile Colombia Mexico Peru	Argentina Brasil Costa Rica Ecuador Uruguay
DECREASING		Venezuela