



**What Hinders Small and Medium
Entrepreneurs in Mozambique?¹**

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ABBREVIATIONS

AAEPI – Associação de Agentes Económicos da Província de Inhambane
AGRARIUS – Associação de Empresários Agrários de Moçambique
AIMO – Associação Industrial de Moçambique
AJAM – Associação dos Jovens Agricultores de Moçambique
AMODER – Associação Moçambicana para o Desenvolvimento Rural
BIM – Banco Internacional de Moçambique
BCI – Banco Comercial de Moçambique
BSTM – Banco Standard Totta de Moçambique
ULC – United Leasing Company
CADI – Centro de Aconselhamento e Desenvolvimento Industrial
CIDA – Canadian International Development Agency
CLUSA – Cooperative League of United State of America
CTA – Confederação das Associações Económicas de Moçambique
DPIC – Direcção Provincial de Indústria e Comércio
EMPRETEC – Empreendedores e tecnologia
GAPI – Sociedade de Gestão e Financiamento para a Promoção da Pequena e Média Empresas or Gabinete de Promoção de Pequena Indústria
GDP – Gross Domestic Product
GTZ – Gesellschaft Technische Zusammenarbeit
IFAD – International Fund for Agricultural Development
IFC – International Finance Corporation
IMF – International Monetary Fund
KfW – Kreditanstalt fur Wiederaufbau
MEDA – Mennonite Economic Development Associates
MIC – Ministério de Indústria e Comércio
MMF – Mozambique Microfinance Facility
MOZAL – Mozambique Aluminium Smelter
MT - Metical
NGO – Non Governmental Organisation
PARPA – Plano de Acção para Redução da Pobreza Absoluta
PODE-CAT – Projecto para Desenvolvimento Empresarial – Componente de Aprendizagem Técnica
RPED: Regional Program on Enterprise Development
SDZ – Sociedade de Desenvolvimento de Zambézia
SMEELP – Small and Medium Enterprises Empowerment and Linkage Program
SME – Small and Medium Enterprise
SOCREMO – Sociedade de Crédito de Moçambique
UEM – Universidade Eduardo Mondlane
UGC – União Geral das Cooperativas
UNAC – União Nacional dos Camponeses
UNCTAD – United Nations Conference on Trade and Development
UNIDO – United Nation Industrial Development Organisation
UPCCM – Unidade de Produção de Castanha de Cajú de Morrupula
US – United States (of America)
USAID – United States Agency for International Development
USD – United State Dollar
VAT – Value Added Tax
WB - World Bank

EXECUTIVE SUMMARY

The Italian Cooperation carried out this study in order to provide a preliminary analysis for the implementation of a project on private sector support, financed by the Italian Ministry of Foreign Affairs. This project has two principal objectives: first, encouraging entrepreneurial sector development; second, facilitating access to credit for SMEs, especially in the agricultural and fisheries sector.

The study intends to show the main constraints faced by SMEs and suggests what should be done to overcome these problems. It also attempts to give some practical recommendations for an effective implementation of the project above mentioned.

A series of linked constraints hamper SMEs development. Improper institutional incentive framework, insufficient capital, shortage of qualified staff, delays in exporting/importing and high transport and power costs cause serious inefficiencies in the private sector.

The analysis is based on structured interviews carried out in four provinces among financial institutions, international organisations, government representatives and private enterprises. On the one hand, those supplying credit ask for an improvement of the entrepreneurial attitude and capabilities. On the other hand, those applying for credit require an improvement of the access to credit characterised by better coordination of the central monetary policy and lower interest rates.

Access to financial resources for SMEs is particularly difficult in Mozambique. The interest rate is very high and the use of financial services is restricted to some privileged entrepreneurs: only 5 percent of all registered firms have access to bank finance with most firms using their own funds for both working capital and investments (World Bank, 2003, p. 6). The formal financial system is unable to finance the economy and when it does, it is skewed towards large and foreign owned firms. All the main financial institutions are highly concentrated in Maputo and in other few urban centres, while the rural areas are often left behind with limited or inexistent provision of financial services (Castel-Branco, 2002).

SMEs are regarded as high-risk and unprofitable investment by commercial banks and other investors, especially in the agricultural sector where the business nature is seasonal and the exposure to unpredictable situations is high. Furthermore, given the higher returns and lower exposure to risk, the banking system considers more attractive the purchasing of treasury bonds than investing in SMEs.

However, although a first overview of the constraints experienced by Mozambican entrepreneurs suggests that difficult access to credit is the main obstacle for starting and developing small and medium firms, one of our main conclusions is that a more in-depth analysis of the current situation of the private sector indicates that the viability of most businesses is hindered by scarcity of entrepreneurial capacities.

Even when SMEs accept to pay for high interest rates, the credit institutions often reject them. Their activities are perceived risky² as a result of lack of entrepreneurial attitude, bad management and structural conditions. It is widely believed that it is essential to invest funds in business services development, including market and industry research, business plan and evaluation, advising and training. Opinions collected during our interviews show that many businessmen fail because they do not have sufficient managerial skills and specific experience in accounting, business plan, quality standards, market strategies penetration and so on.

Hence, we recognise that in order to promote SME development it is essential to facilitate SME use of financial services and assist them with the provision of business development services in terms of marketing and advisory support, training and forging linkages between partner businesses. The rationale of this intervention lies in the difficult identification of sectors and businesses with high market potential. Besides training on business management, information about technological aspects of the activities they run or they think to start running should also be provided. For instance, people involved in the agricultural sector ask for assistance in agricultural practices, forestry management and fishing methods.

Another argument of this study is that, in order to foster private sector, we need a development strategy for SMEs able to harmonise the different existing initiatives in favour of small and medium sized companies. There is urgent need for a clear policy to support SMEs. This policy should adapt to the Mozambican context and complement with other policies related to the industrial, agricultural and commercial sectors.

The Italian Cooperation should coordinate its project with the other activities financed by international and local organisations. While supporting SME development, it should also take into account the policies elaborated by the Government of Mozambique, in particular MADER, in order to promote production and commercialisation of strategic products (e.g. rice, bananas, pineapples etc.) that could be sold both domestically and abroad. We suggest that the Italian Cooperation provides a comprehensive package of support that includes not only credit but also technical assistance in terms of technology, production, market strategy and information.

² Interview with Esmael Osseman, União Nacional dos Camponeses, with Monika Branks, Verde Azul Consulting and with Ia Patterson, AMODER.

1. Introduction

The Italian Cooperation carried out this study in order to provide a preliminary analysis for the implementation of a project on private sector support, financed by the Italian Ministry of Foreign Affairs.

This project has two principal objectives: first, encouraging entrepreneurial sector development; second, facilitating access to credit for SMEs, especially in the agricultural and fisheries sector. Credit is targeted to small and medium sized companies affected by the flood in 2000³.

The rationale of supporting SMEs lies in the willingness of achieving poverty reduction, increasing economic production and obtaining local empowerment. However, recent literature (Biggs, 2003, and Hallberg, 2003) shows that SMEs are not always able to generate more employment, better labour conditions and have a greater impact on poverty reduction than larger firms. In this study we reckon that the main reason for assisting SMEs in Mozambique is that although they form the majority of the economic activity and constitute the main source of employment in the country, their development is hindered by a wide range of constraints. Despite the difficulties to define what SME means⁴, working with small and medium firms is particularly important, since they are highly representative of the Mozambican economy: out of 28.870 enterprises, 28.474 are SMEs (World Bank, 2003)⁵.

Mozambique presents some successful cases of SMEs that have managed to become competitive and highly productive through the technical assistance of specialized financial institutions. They include *Miranda Cajú* and *Unidade de Produção de Castanha de Cajú* of Morrupula (UPCCM) in Nampula province, SDZ in Zambézia MOCIT/Citrum in Maputo province, *Cooperativas dos Apicultores* in Maputo province, TCM Transportadores in Sofala province and Optima in Chimoio and Manica. Moreover, Mozal⁶ during the Smelter Expansion Phase in 2002 and 2003 gave the opportunity to SMEs to work with very large projects through the

³ The flood in 2000 affected more than 4,5 millions of people, living mainly in six provinces: Maputo, Gaza, Inhambane, Sofala, Manica and Tete. Agricultural production reduced by about 20 percent.

⁴ The definition of SME varies from country to country and sector to sector. The most commonly used indicators are: number of employees, scale of operation, annual profit, medium time of internal financial sustainability. In Mozambique we found three commonly used definitions of SME, given with reference to the number of employees.

Agency/Institution	Small	Medium
Instituto Nacional de Estatística (INE)	<10	11-50
Ministério de Indústria e Comércio	25-124	125-249
GAPI	10-50	50-100

Source: World Bank, 2003 and GAPI

⁵ In this study the World Bank adopts the definition of SME, provided by the National Institute of Statistics.

⁶ Mozal is an aluminium smelter that represents the largest investment (about \$US 1.34 billion) ever done in Mozambique. This investment is a consortium owned by London based Billiton (47%), Mitsubishi of Japan (25%), South Africa's Industrial Development Corporation (24%) and Government of Mozambique (4%). Now it doubled his capacity constructing the second smelter and expects to produce 506.000 tons of aluminium per year for exporting reasons.

Small and Medium Enterprises Empowerment and Linkage Program (SMEELP).

This experience showed that SMEs could grow, acquire knowledge and potentially achieve financial independence, if well integrated with projects receiving FDI⁷. However, some of entrepreneurs interviewed underlined that not all the SMEs took advantage at the same level from SMEELP or similar programmes.

A series of linked constraints hamper SMEs development in Mozambique. Insufficient capital, shortage of qualified personnel, delays in exporting/importing goods and high transport and power costs cause serious inefficiencies in the private sector. Also, access to financial resources for SMEs is particularly difficult in Mozambique. The interest rate is very high and the use of financial services is restricted to some privileged entrepreneurs. Currently, the growth of SMEs depends on separated and fragmented programmes, pursued by government, donors, NGOs and international organizations.

The aim of this study is to show the main constraints faced by SMEs, with focus on credit market, and suggest what should be done to overcome these problems. We also attempt to give recommendations for an effective implementation of the private sector support project financed by the Italian Ministry of Foreign Affairs.

The analysis is based on a literature review and structured interviews (see annex 2) made both to financial institutions, international organisations, government representatives and to private enterprises. Interviews have been carried out in four provinces: Maputo, Inhambane, Gaza and Sofala, and to sum up, 32 enterprises and about other 30 different organisations have been interviewed during the period between October and December 2003. The questionnaire mainly focuses on three topics: the credit history of the entrepreneur, other constraints faced by the enterprise and his/her personal opinions about how to improve financial institution supply for SMEs.

One of the main findings of this study is the striking dichotomy between the two types of subjects interviewed. On the one hand, those supplying credit ask for an improvement of the entrepreneurial attitude and capabilities. On the other hand, those demanding for credit require an improvement of the access to credit characterised by better coordination of the central monetary policy and lower interest rates. The high cost of capital basically includes the difficulties of the two sides market.

We first suggest that providing specialized technical assistance may be fundamental towards an interest rate reduction, by decreasing the risk premium. This would correspond to a reduction of the risk run by banks and investors, who currently refuse to work with low qualified entrepreneurs. Business development services may contribute to develop entrepreneurs' skills and ensure the good performance of their economic activities. However, we should bear in mind that market rates also highly depend on the monetary policy.

⁷ Mozal Dois, *Jornal de Circulação Interna*, 16 de Maio de 2003.

In addition, it is required an acceleration of the reform agenda concerning the legal and regulatory framework for the private sector. It is unlikely that financial institutions are going to trust SMEs and vice versa, if enforcement contracts are not guaranteed.

The report is structured as follows. First, we examine the situation in which SMEs operate and we collect information on the factors that create inefficiencies in the business environment. Then, we analyse possible interventions to enable private sector development and, in particular, we provide recommendations to accomplish the objectives pursued by the project that Italian Cooperation will implement in 2004/05. Moreover, we analyse the offer of the existing SME support programmes by presenting a general profile of the principal technical assistance providers. Finally, we draw some conclusions.

2. Constraints for SMEs development

Small and medium sized companies meet a wide range of obstacles to their development. On the basis of what reported by those interviewed, we classify these constraints into four groups:

- credit market
- macroeconomic environment
- institutional framework
- infrastructures and market

2.1 Credit market

Market economies develop from private investment. Private investment needs to be financed and financing implies access to credit. Credit can originate from both capital markets and commercial bank sector.

In Mozambique both capital markets and banking sector appear to have relevant problems. On the one hand, the capital market is scarcely developed. On the other hand, credit by commercial bank system is highly constrained. Although the remarkable presence of credit lines (banks, registered credit institutions, credit cooperatives etc.)⁸ and international financing sources in the country, it is evident that the access to them is still very limited.

According to people interviewed, capital low access determinants may be found in both the demand and the supply side of the SMEs credit market. SMEs face both financial and non-financial constraints that exclude them from the financial system.

The first *supply side* constraint is definitely the excessive cost of capital (interest rates, real guaranties, commissions and taxes) compared to the low return of investment. During our interviews most entrepreneurs said that they do not even try to approach commercial banks because they

⁸ See appendix I in order to have further information on the existing financial institutions.

know to be unable to pay the required interest rate. Entrepreneurs stressed that government should subsidise credit to selected enterprises until they reach their own viability.

Small and medium entrepreneurs make use of commercial banks only to deposit their savings. Any other financial service is not exploited, because they are not aware about other opportunities, such as microfinance institutions. They usually started their firms and keep making investment by using exclusively their own capital or approaching informal sources of credit, such as moneylenders, relatives and friends.

Leasing represents an exception for some entrepreneurs in Beira and Maputo. Few applied for a leasing to buy their equipment: machineries, computers, desks etc. They made this choice because of the lower interest rate, no collateral requirement and longer repayment period. However, we should notice that this product is not available for those involved in the agricultural sector, it is provided only by large financial institutions, such as BIM, BCI, BSTM and ULC, and all the bought equipment has to be insured. Only entrepreneurs in urban centers know what leasing is and how it works. People asking for a leasing are usually those able to pay back in dollars. That is why the interest rate is much lower.⁹

SMEs have insufficient collaterals to offer to the financing system in order to get a loan. According to a World Bank study (2003), short and long-term loans require collateral up to 300 percent. Land cannot be used as collateral because private ownership is prohibited in Mozambique. Furthermore, acquiring land use rights is time-consuming and expensive. According to Regional Program on Enterprise Development (RPED) 2002, it costs about \$ 18.000 and takes one year. The current reform entails that land can be acquired by 50 years lease concession and renewed 50 years further, paying an annual leasing fee to the Government. However, it has not yet a commercial value and, hence, cannot be used as collateral. The real guarantees required by the financial institutions appear excessively demanding: about 120 percent of the loan has to be guaranteed by real assets (Iacovone et al., 2003).

The capital market is also a good example of an (almost) completely missing source of capital. When commercial banks are not able to finance the entire economy, an alternative source is usually represented by capital market. However, in Mozambique the stock exchange market (BVM) started operating in 1999. So far, about 12 large companies are registered in the BVM. Moreover, a proper class of brokers is missing and the number of industries whose securities could be traded is still restricted. The promotion of stock exchange market has been supported by the privatisation of some state owned enterprises, but it is not yet robust and does not reach broad based participation. Many companies are, in fact, excluded from this market because of its restrictive entry conditions.

From the *demand side*, access to credit is constrained by limited entrepreneurial capacities. We think that those capacities are limited by an inefficient institutional framework and lack of experience. Each of these features affects the other.

⁹ The interest rate for a leasing in dollars is about 9-10 percent per year, whereas for the same leasing in meticais is around 35 percent (interview with SCA in Beira).

First of all, the institutional set of rules in the Mozambican society was shaped in a context characterized by centralised and widely non-monetarized economy. The recent transition process to a market oriented economy has been slowed down by the pre-existing unwritten and informal rules. Institutions are not yet market-efficient and this leads to high transaction costs for SMEs.

Enterprises face serious internal problems like need for modern technology, incapacity to exploit scale of production and employee expertise. Those interviewed experience the lack of appropriate qualifications, equipment, techniques and information as crucial obstacles. Business management training (sustainable business plan and market strategy, transparent accounting system, level of indebtedness consistent with their own capital) and technical and vocational training are essential to meet bank requirements for the concession of loans and for facilitating a general access to the financial sector. In order to address these challenges, development of specific services and products for SMEs such as venture capital, leasing, loan insurance and mutual guarantee companies has been gradually promoted.

Commercial banks are highly risk-averse. SMEs, especially in the agricultural and agro-industry sector, are negatively discriminated because of their lower returns, higher risk and longer period of recovery in comparison with other economic sectors, such as trade and services. Agricultural entrepreneurs stated that they face high obstacles to get credit from official financial institutions. In Carvalho Neves (2003) we found the following distribution of credit to different sectors: 35 percent to industry, 49 percent to commerce and other economic activities and only 16 percent to agriculture. Those questioned reported that banks should have the social responsibility to share risk and costs with entrepreneurs. Credits institutions highlighted, on their side, the high proportion of non-performing loans (25 percent of portfolio) and limited creditor enforcement of contracts.

Moreover, asymmetric information between creditors and debtors generates high uncertainty in the business environment. Then, to reduce the risk of failure, lending markets establish remarkably high interest rates and credit is skewed towards larger and foreign owned firms. In order to expand their power and achieve their own interests, banks make strong linkages with well-established companies rather than SMEs, which are seen as inefficient, risky and therefore not creditworthy.

A further issue is that savings are limited. They account for about USD 900-1000 millions that are 30 percent of the GDP (Iacovone, 2003). Mozambican banks control only 15-16 percent of the entire financial system, while foreign investors manage all the rest¹⁰. Such a low deposit level is unable to finance all the productive sectors. It is evident that a country with low level of savings and without entrance of foreign indirect or direct investment, it encounters serious difficulties in financing its investment. Only large and well-established companies have the required negotiation power to get credit, while new or reduced scale enterprises are excluded from the official financial circuit.

¹⁰ Interview with Castel-Branco (2003)

2.2 Macroeconomic Environment

The GDP growth rate is not a self-explaining figure. It is important to investigate to which extent economic growth is linked to the private sector growth or it is spread out all around the country. In Mozambique, the GDP growth rate is strongly affected by external aid and mega-projects (owned by foreigners) contribution, which according to Castel-Branco (2003b) accounts for almost half of the entire growth rate.

The macro-economic adjustment, which took place in the last fifteen years, led the local economic system to an internal macroeconomic stability both in terms of prices, which are well represented by the inflation and the exchange rate¹¹, and in terms of public finance institutions stability, as it is shown either by the level of the internal and external debt¹² or by the general public finance sustainability¹³.

The Central Bank, which is the guarantor of monetary and economic stability, keeps under control the prices growth (inflation) and the stability of the banking system (compulsory reserve requirement). In both the cases, it may restrict the supply of money. The monetary policy is complicated by a high dollarisation of the economy, by the foreign budget support and by foreign aid expenditures outside the budget. In 2000, moreover, the crises of the two major banks, Banco Commercial de Mozambique e Banco Austral, has been followed by a large public re-capitalisation, financed by Treasury bonds operations. This basically increased the interest rate (the price of Treasury bond) and reduced the national monetary base.

Tight monetary policy led to high interest rates that prevent entrepreneurs from gaining access to the capital. It is well known, indeed, the trade-off between the interest rate and the national monetary base, where a reduction in the latter increases the first. Besides, a high interest rate generates elevated returns from financial asset, which definitely changes the investment opportunity portfolio between commercial and financial activity. In practice, commercial banks perceive more convenient to have predetermined return on Treasury bonds than to invest on risky SMEs operations.

Clear strategies, guidelines and complementary measures to make viable investment on the SME sector have not been yet adequately defined. Both industrial investors and banks are unwilling to risk on SMEs because of the absence of explicit policy directions and mechanisms of strategy implementation on this sector.

¹¹ The continued strengthening of the South African Rand has contributed to inflation pressure during last year.

¹² The most recent FitchRatings report (2004) put Mozambique in the B rating category although external debt indicators are high relative to this rating category. Accordingly to the report, the risk of external payment crises is mitigated by the fast declining trend of the external debt ratios and because the nominal debt increase is mainly related to the FDI borrowing from private sector.

¹³ Foreign financing support still accounts for a very high share of the total revenue (around 40%), but is mainly in form of grants. Tax to GDP ratio is still low (projection for 2007-08 are at around 17%-18%), but it is positively growing.

Table 1. Monetary market – Selected indicators

	2000	2001	2002	2003
Growth rate GDP (%)	1.5	13.0	8.3	7.1
Cumulative inflation rate (% , December)	11.4	21.9	9.1	13,8
Annual average inflation rate (%)	11.4	9.1	17.1	13.4
Exchange rate MT USD (Annual Average)	15,141	20,454	23,180	23,341
Exchange rate MT Rand (Annual Average)	2,192	2,504	2,266	2,915
Exchange rate MT Euro (Annual Average)	353	372	21,896	26,361
Balance of Payments (millions of USD)	-827	-623	-760	-608
External Debt (millions of USD)	5,125	5,123	3,702	3,989
Monetary Base (Balance Annual Var. , %)	na	na	17.4	22.0
Interest rate of BM intervention (Standing Lending Facility % , December)	na	35.4	26.5	18.5
Treasury Bills 182 days (Average of Interest Rates for the last six Auctions, December)	na	32.1	28.0	13.2
Interest rate MAIBOR 6m (% December)	na	36.3	33.2	28.9
Interest rate MAIBOR 12m (% December)	na	36.5	34.6	30.2

Note: BM (2004), NA not available

2.3 Institutional Framework

“Institutions are the rules of the game in a society or, more formally, are the humanly devised constraints that shape human interaction. In consequence they structure incentives in human exchange, whether political, social, or economic. Institutional change shapes the way societies evolve through time and hence is the key to understand historical change” (Douglass North, 1990).

In this section we focus on how constraints in the formal institutional framework may hinder economic activities development. We basically refer to the business registration costs, bureaucratic process, contract enforcement procedures, sharing information lack, labour regulation, commercial code and so on.

The new policies in favour of the private sector (e.g. provisions for industrial free zones) face obstruction in their implementation. Local officers often delay or ignore the new policies, by making them ineffective (RPED, 2003). Before releasing an industrial license, MIC requires for a full drawing of installation, topographical map, detailed description of the employees and environmental impact analysis (UNIDO, 2003). This is a standard procedure in any country, but the problem is that it results very costly, in particular for small entrepreneurs. This is the main reason why many economic activities remain unregistered, with the obvious consequence not to be able to access official credit institutions¹⁴. The few that manage to get a registration, have also to apply for a number at the tax department, get work, residence and imports permits and open a bank account.

¹⁴ In this sense, microfinance institutions may constitute an exception.

Information about business related laws and administrative procedures are limited. Entrepreneurs are often unaware about new technologies, internal and international standards and new potential markets. Business associations are expected to facilitate information sharing on technologies, market opportunities, access to capital etc. We interviewed some of them operating in Mozambique, such as AJAM (Associação Jovens Agricultores Moçambicanos), ACIS (Associação Comercial e Industrial de Sofala), ACB (Associação Comercial de Beira). They reported that they face major difficulties to reach SMEs and denounce the high corruption level in the legal and administrative sector.

Lack of a clear labour law regulating market is a restraint that implies excessive costs of doing business. Most Mozambican firms have a work force larger than their needs, while the informal market of labour contracts largely spreads out. The new labour law for foreign experts (decree 57/03¹⁵) adds a further ambiguous component to the current legislation: the Labour Minister and his technical staff can discretionary decide how many and which foreign workers to be hired in each Mozambicanian firm. Some of those questioned said that dealing with the Inspectorate of Labour is one of the reasons that prevent people from investing on Mozambique.

Business tax obligations are confusing and not transparent¹⁶. For instance, the VAT repayment system¹⁷ is not yet working well, since the late refund to the companies (on average 99 days, World Bank, 2003). This obviously does not facilitate the growth of business start-ups in Mozambique. Many companies never received refunds on VAT-exempt products or exported products. Insufficient coordination between national and local tax authorities creates inefficiencies in the fiscal system with a negative impact on SMEs.

A clear legislation about bankrupt firms does not exist. This is unhealthy for the whole business environment. The official law in Mozambique does not force a borrower to be responsible for credit he/she gets. No sanction takes place against the insolvent borrower and when it does, the claiming procedures are costly and time-consuming for the lender. Letting off defaulting debtors too readily may discourage potential creditors because of moral hazard. This means that entrepreneurs may take greater risks than they would do if an enforcement law were in force. Currently, lack of such a law leads banks to be extremely selective with their clients. There is urgent need for a law that insures obedience to the contract.

Finally, a comprehensive lack of trust in the Mozambicanian legal system emerges from the interviews. Any product is available without any tax enforcement in the informal market. Smuggled products represent a real hindrance for legal sales. There is quite limited trust on business associations and many firms consider them helpless and concentrate in solving problems of specific groups of interest. Many entrepreneurs also

¹⁵ The Government is actually reviewing the law, which will only be submitted to the Parliament during the next legislature (political election in December 2004).

¹⁶ There are over 30 direct taxes (World Bank, 2003)

¹⁷ The Value Added Tax is 17 percent and is levied on transactions including imports of goods, non-gratuitous transfer of goods and provision of services.

think that government should not manage donors' funds because they would use them in favour of their close friends/relatives.

2.4 Infrastructures and Market

The long period of civil war destroyed the limited infrastructures that Mozambique inherited from colonialism. Infrastructure lack slows down the development of SMEs. Most of those interviewed stated that transportation problems and electricity interruptions have a severe effect on the productivity of their firms and commercialisation of their products.

Despite the country has potentially a good transportation network through three corridors: Maputo-South Africa, Beira-Zimbabwe and Nacala-Malawi, rural zones are isolated from the urban areas and are characterised¹⁸ by an insufficient availability of roads, bridges, irrigation and electricity system. The sea route is a natural advantage for trading. However, inefficient shipping companies and clearance delays impede a full utilization of it. The reconstruction of the transportation infrastructure system is fundamental for waking up the private sector in Mozambique.

This is particularly serious in the North of the country. The floods of 2000 and 2001 worsened the roads situation in Mozambique, in particular in the provinces of Gaza, Inhambane, Maputo, Sofala and Manica. The direct implication of this geographical remoteness is that the transportation costs become very high and in order to compensate for them, commercial dealers transfer these costs to their customers by increasing the prices of the processed agricultural products.

Some interviewees said that the main rivers in Mozambique could be a great potential for agriculture, if adequate infrastructural investment to make them navigable are done. In addition, lack of an appropriate irrigation system might transform them in a dangerous threat. During the rainy season, they can overflow and destroy the entire cultivation. Financial institutions should provide farmers with some forms of insurance against these events.

Electricity is another major problem for SMEs. Power cuts are frequent and they obviously cause decreases in productivity. Only few firms have their own generators.

Despite the barriers listed above, there are some initiatives that are attempting to reduce constraints for SMEs development. The private sector, Government of Mozambique, donors and international organisations undertake these initiatives. The Enterprise Development project has had some success in helping small- and medium-sized enterprises, with capturing \$30 million of business from mega projects per year. However, it is fundamental that the different SMEs development activities are organised with coordination and conceived strategically.

It is important to highlight that one of the main infrastructures often missing in the country is the market itself. We do not only refer to physical places where to commercialise goods, but also to more complex

¹⁸ National Human Development Report, 1998

networks of goods and services exchanges, which normally exist in more advanced economies. This kind of infrastructures encounters difficulties to grow because of limited physical infrastructures, like transports, but also because of a lack of trade attitude in “people mentality”.

3. How to promote private sector growth

We are now going to argue about what can be done in order to address the most binding constraints faced by SMEs presented in the previous section. The discussion is based on the suggestions provided by those interviewed, including both entrepreneurs and SME experts.

Although a first overview of the constraints experienced by Mozambican entrepreneurs suggests that difficult access to credit is the main obstacle for starting and developing small and medium firms, a more in-depth analysis of the current private sector situation indicates that the viability of most businesses is hindered by scarcity of entrepreneurial capacities.

Even when SMEs accept to pay for high interest rates, the credit institutions often reject them. Their economic activities are perceived risky as a result of lack of entrepreneurial attitude, bad management and structural conditions. It is widely believed that it is essential to invest funds on business services development, including market and industry research, business planning and evaluation, and management training. Opinions collected during our interviews show that many businessmen fail because they do not have sufficient managerial skills and specific experience in accounting, business plan, quality standards, market penetration strategies and so on. It is important that credit supply is always supported by technical assistance services that can direct loans towards competitive and productive investments. Training courses need to be: (i) heavily subsidised in order to attract costumers; (ii) available in all provinces; and (iii) able to fill in the gaps between the education system and the needs of private firms.

Besides training on business management, information about technological aspects of the activities they run or they think to start running should also be provided. For instance, people involved in the agricultural sector ask for assistance on agricultural practices, forestry management and fishing methods. This type of knowledge can be acquired by learning from others through joint ventures and outgrowing. This could allow small and medium entrepreneurs with updated information about new technologies and strategies that may enable them to upgrade their business.

A possible way of upgrading SMEs is through the creation of vertical integration agreements with either larger local firms or international companies (Castel-Branco, 2003). SMEs can adopt both vertical and horizontal integration strategies in order to grow quickly and reduce their costs. This means: *“enterprises are connected to others in networks of exchange. Through networking organisation can access complementary resources and/or capabilities or can closely coordinate their use of resources; in this way, they hope to enhance their competitiveness, for*

example in terms of improved products, better market access or faster market enter and thus increase their revenues” (Ebers, 1997, p. 6). They could get subcontracts with large and experienced companies, make medium and long-term partnerships or become a branch of similar or complementary industries.

Instead of competing with each another, enterprises may grow together by making medium and long-term contracts, sharing capacities and information, and conducting market research. Integration is not only a way of increasing profit by reducing costs, but also strengthening internal capacities, accelerating the learning process about new technology and ensuring stability of the economic activity. If a small or medium sized firm is integrated with a big and influential company (e.g. Mozal, SASOL, Western Mining), the latter power or reputation can help the small one to achieve its objectives including getting medium and long-term loans from financial institutions.

Working with business associations¹⁹ could be another effective method of building up capacities and reaching a broader number of firms. This is also significant both to improve the dialogue between the private sector and the government and to speed up the legal system reform process. These associations could lobby the government to remove some of the above-discussed constraints. For instance, they could make pressure to make financial institutions collect their deposits. Many entrepreneurs complain not to have a safe place where to put their savings. Moreover, business associations might be a valuable channel through which spread information about technology, market opportunities, international quality standards, laws and other legal procedures. However, we also acknowledge that business associations need themselves capacity building and specific training in order to assist efficiently SMEs.

There is no development bank in Mozambique. Experience from other countries shows that specialized small enterprise banks, division of development banks, credit unions and cooperatives can be effectively used to deliver funds for small and medium firms (Lieldholm, 1998, p. 426). Some interviewees²⁰ proposed that these development-lending institutions may also be strengthened in Mozambique through a common action of the local government and international organisations. They could offer their loans at lower interest rate so to force commercial banks to decrease the cost of the lent money.

One of the most interesting experiences of cooperatives in Mozambique is the União Geral das Cooperativas agro-pecuarias (UGC). The UGC is composed of a large number of cooperatives that work in the agricultural sector, including farming and processing. The cooperatives' workers can benefit a series of coordinated programmes that offer both education and health services and savings and credit facilities. The union is based on an individual production model and shared ownership of the essential production tools. UGC refers to UNAC (União Nacional de Campones) which plays an important role of coordination among all the Mozambican

¹⁹ Most of the associations are confederated with the CTA (Confederação Associações Económicas de Moçambique), which is gradually assuming an important firms representative role.

²⁰ José Negrão from Cruzeiro do Sul, Gustavo Miranda and Fidelx Kulipossa from GAPI

cooperatives, financial intermediation between donors and farmers, leaders training of local associations, provision of equipment and support in the construction of infrastructures.

In Mozambique some organisations, including GAPI, AMODER and TechnoServe, play an important role in helping SMEs to obtain loans and improve their entrepreneurial skills with technical assistance. At this stage, SMEs do not have the capacity of developing themselves, they need internal and external institutions that can mobilise funds at reduced interest rate, long repayment period and provide business development services at low prices.

It is necessary to create incentives for local financial institutions motivated to target SMEs. Currently, it seems that only two financial institutions, GAPI and AMODER, are keen on working with small and medium agricultural enterprises. Therefore, particular support ought to be given to those organisations willing to operate in the rural areas. This kind of intervention would be in line with two of the priority areas highlighted by the Mozambican Poverty Reduction Strategy Paper, the PARPA (Plano de Acção para Redução da Pobreza Absoluta): rural development and enforcement of the financial and macroeconomic system.

If SMEs support is a priority in the development process in Mozambique, then it is fundamental to strengthen the linkages both between rural and urban areas, and among different sectors. The construction of new roads, bridges, electricity networks should be strategically thought in order to facilitate the growth of industrial and commercial activities in the country. There is a clear lack of investment in appropriate physical infrastructure.

In addition, the bank system should mobilise its funds, while the government should ensure a legal environment necessary to protect banks and SMEs, subsidise credit and offer non-financial services.

The juridical system needs to be simplified in order to reduce transaction costs for the registering and licensing process of a company. A feasible solution could be to keep supporting and improving the creation of one-stop shops or Balcão Unico²¹, where the entrepreneurs can go to have done administrative procedures, such as licensing and taxation. This would be especially valid in provinces where access to information is limited.

Given that there is no explicit policy in favour of SMEs, the government should act directly by developing policy strategies that can make these SMEs attractive to banks and other investors. Furthermore, it is also supposed to protect the infant industry by defining clear goals, interventions tools, criteria and performance indicators that each enterprise ought to achieve within a certain period of activity.

Considering the Mozambican extensive agrarian base, one of the key areas where to operate should be the agro-industry, including fisheries (Política e Estratégia Industrial, 1997). The existing agro-industries are mainly micro and small. They face serious problems in terms of shortage of raw material, infrastructures and entrepreneurial culture.

²¹ The project has been already implemented in two provinces and the government is working on a unique national model that can be applied in all the provinces.

Industrialisation and agricultural production are profoundly disarticulated. The information network about opportunities, technology, innovation is limited, informal and scarcely useful.

Hence, clear agro-industry policies are urgently needed in order to help SMEs to grow in this sector. Government of Mozambique, entrepreneurial associations, donors and other financial actors need to harmonise their actions and strategies and make a real effort to implement them. Disintegrated and autonomous programmes risk being ineffective or, in the worst perspective, slowing down the development process of SMEs. This is why there is need to develop a comprehensive SME policy.

Competitive investments should be accompanied by complementary investments, able to foster competences, capacities and sustainability of small and medium firms. However, when this is not possible, it is necessary to define how firms with competitive investment should behave, how to reduce their predator competition and create new partnerships that make them strong and successful. The industrial policy needs to be a clear guide of private sector development, a tool for discussion, implementation and coordination of the different interest groups in the society.

4. The Italian Cooperation programme and the private sector in Mozambique

The analysis of both the above discussed constraints and the impressions of the questioned entrepreneurs allowed us to reach some conclusions about how to increase the productive capacity of small and medium sized companies and improve their access of credit.

In particular, in this section we would like to provide the Italian Cooperation with some suggestions about the implementation of the project on private sector support and discuss some theoretical and empirical ideas about how to develop SMEs in Mozambique.

The project targets at least 100 enterprises affected by the flood in 2000. The flood affected approximately 40 districts in five provinces, namely Maputo, Inhambane, Gaza, Manica and Sofala. This means that on average the project ought to reach 2 or 3 enterprises in each district. More than fifty percent of these economic activities should be involved in the agricultural sector, including provision of inputs, commercialisation and transformation of agricultural products.

DPIC (Departamento Provincial de Industria e Comercio) in Maputo Province and Maputo City suggested that the project should reduce the number of targeted enterprises and focus on few districts. The reason for this is to guarantee that the targeted enterprises have adequate support and are able to be self-sustainable in the long term. The concentration of the activities on few and specific districts would allow to create the necessary conditions to develop linkages among firms. The identification of the districts should be carried out on the basis of its economic opportunities, accessibility and seriousness of the damages made by the flood. Given all the constraints mentioned above, both small and medium

companies and the selected financial institutions working in rural areas need constant and close supervision.

Restricting the number of districts will not only correspond to an effective use of resources and time, but also to an easier performance monitoring that should prevent enterprises from failing at the end of the programme. The challenge is to guarantee sustainability of the project, while outreach will be improved at a further stage. Credit is a valid means to support private sector. However, more attention should be given to technical assistance. Training and counselling for both entrepreneurs and financial institutions is essential to ensure a successful management of the funds.

We believe that the provision of loans and business development services is complementary. Entrepreneurs ask for technical assistance at low cost and focus on basic knowledge about accounting, computer and other technical aspects. They complain that most of the current training courses (e.g. PODE-CAT) are too expensive and advanced. The provision of business development services should also reduce the risk seen in the agricultural sector.

In the following section, we will provide a list of the existing SME support initiatives that might be consulted in order to overcome the absence of technical assistance in the project. If it is not possible to introduce this component at this stage, it is recommended that a new project on business development services for SMEs is implemented as soon as possible.

The evaluation of this intervention should consider not only the number of given loans and their repayment rate, but also how much enterprises have enhanced their productive capacity through increases of their profits and investment on new equipment, commercialisation of their products, staff development etc. We think that these indicators should be included among the expected results.

The project defines that the loan maximum amount by firm should be equal to USD 100.000. We suggest that the loan average amount should be lower, in particular for agricultural enterprises. Most of the interviewed enterprises reported to need an amount between USD 2000-4000 in order to finance their own activities. There was only one entrepreneur that declared to need about USD 600.000, for expanding its company. On average, small and medium entrepreneurs are afraid of large amount of money. They think not to be able to manage and pay it back.

We recognise that the subsidised interest rate is essential to stimulate the Mozambican private sector. The current interest rate applied by commercial banks pushes out entrepreneurs from the official financial circuit. Without this help, infant economic activities would not be able to start-up and make investment, in particular in the agricultural sector.

Many entrepreneurs argue that funds should be directly allocated to their companies, without passing through the management of MIC. They fear that money may be centralised in Maputo and/or given exclusively to influential companies. We underline that the steering committee, including the representative of the Italian Cooperation, plays a fundamental role to ensure the impartial and punctual provision of the loans.

It is recommended that an effort be made to reach those firms that did not take part to the USAID project²². During our visits in the field, we notice that there is need to diversify the funds allocation. The activities involved in the USAID project have already recovered from the emergency and fully restarted their business cycle, while those ones remained out are still in need.

Repayments are more secure if credit is given through an intermediary such as business associations, cooperatives and community based organisations able to convey the culture of repayment and sense of responsibility. For example, most entrepreneurs do not have money for buying a machine like a tractor, while a business association or cooperative can purchase it by asking for a credit and then pay it back through the fees applied for renting the machine to its members. Collective credit solves the problem to reduce the repayment risk in the SME sector. This argument is particularly true for agricultural firms. Some of the existing entrepreneurs associations have influence and credibility to develop collective actions in favour of the local private sector and affect the behaviour of their members. Furthermore, they could facilitate information sharing among the entrepreneurs.

While supporting SME development, the Italian Cooperation should take into account the policies elaborated by the Government of Mozambique, in particular MADER, in order to promote production and commercialisation of strategic products (e.g. rice, bananas, pineapples etc.) that could be sold both domestically and abroad.

If possible, funds should be allocated to enterprises that are working in the same product chain. This would allow forging linkages among different and complementary activities. For example, loans could be directed to sellers interested in buying agricultural goods from farms already involved in the project. Financing isolated activities might lead to failure. MIC should act as facilitator by identifying potential partners and inducing them to collaborate and share information and resources.

Finally, we experience difficulties in the identification of established enterprises in the agricultural sector. Most agricultural activities operate in the informal sector. They usually are household farms that consume what they produce. This limit should be addressed by working closely with the district departments of Agriculture and business associations. They are the best partners to offer complete and updated information about the local entrepreneurial situation. In addition, despite the incentives presented in the project, it might be complicated to contract financial institutions willing to direct their credit to agricultural SMEs.

5. Existing SME Support Programmes

A careful analysis of the answers given by both entrepreneurs and financial institutions shows that, what is required is a strong link between loan concessions and specialized commercial and financial training

²² USAID has implemented a similar private sector support programme of about 20 millions of USD during 2002/2003.

services. They are important to build internal capacities and ensure the sustainability of the small and medium firms in Mozambique.

This section describes the principal programmes supporting private sector and, in particular, SMEs development by offering technical and vocational assistance. They mainly provide:

- Strategic planning advice
- Business management training, including administration of a transparent accounting system
- Formulation of business and financial plan
- Business counselling on project development
- Advisory services on company organisation and legalisation
- Provision of information on market opportunities, laws or other rules related to business
- Forging linkages between partner businesses

A wide range of actors, including government institutions, bilateral and multilateral agencies, local associations, NGOs and consulting firms, offer these services. We do not pretend to provide a complete list of all the SMEs support initiatives in the country, but the main ones suggested by the questioned entrepreneurs and SME experts.

5.1 Projecto para o Desenvolvimento Empresarial - (PoDE-CAT)

The World Bank supports the PoDE-CAT project with a credit line of US\$ 26 millions (the project is moving from a full subsidy system to a 50 percent granting), which aims at promoting Mozambican entrepreneurs through three components:

- Componente de Aprendizagem Técnica (CAT) that offers training, advisory, marketing services to SMEs in order to build up their technical capacities and increase competitiveness skills.
- Financing private medium term investments on sectors, including tourism, agri-business, services, transportation and industry.
- Institutional capacity programme to improve the public-private consensus.

During the interview with the director, it has been reported that PoDE initially financed few projects directly. Most of the funds were given to commercial banks that require the same interest rate they apply to their funds. Currently, the credit line is supporting the establishment of risk capital funds. PODE created equity funds, where the best entrepreneurs are selected and manage privately the fund. They share 50 percent of the risk and 50 percent of the profits. The World Bank is strongly convinced that there is need for modern business practices, such as venture capital and leasing, able to foster SME sector development.

CAT, the component dedicated to technical assistance, seems to be quite effective. Consultancies and training courses for enterprises are generally subsidised by 50 percent, while entrepreneurs pay the remaining 50

percent. Until June 2003 CAT supported 217 projects by providing 55 percent of assistance in Maputo and the remaining 45 percent in the other provinces.

One of the main criticisms raised to this project concerns the high cost and advanced level of the courses provided. Small entrepreneurs, in particular, cannot benefit this opportunity because they cannot afford this cost.

5.2 Enterprise Mozambique

This initiative of CTA and the Government of Mozambique aims at establishing and consolidating the Mozambican private sector. It is supported by UNDP and provides a wide range of services, including workshops for entrepreneurs, consulting and forging linkages among firms. This programme:

- Identifies promising entrepreneurs;
- Conducts training aimed at developing entrepreneurial traits and business skills;
- Assists companies in accessing financial and non-financial services;
- Encourages the exchange of experiences and networking among programme's participants both locally and internationally;
- Helps to arrange mutually beneficial links with national and foreign companies;
- Puts in place long-term support systems to facilitate the growth and internationalisation of their ventures

The core aim of Enterprise Mozambique is to facilitate entrepreneurship development, including capacity building in technology, management, exporting, and networking.

5.3 Cooperative League of the United States of America

CLUSA is a financial institution²³, which provides loans in order to support the commercialisation of smallholder production in Mozambique. Since 1995 it works mainly in the Nampula province by developing farmer associations, cooperatives, business groups and other economic organisations and strengthening relationships between them.

CLUSA also offers technical assistance to its associated. Farmers are motivated to develop sense of ownership and direct responsibility of their economic activity. They are trained on business plan and management, accounting systems, doing networking. Experience shows that the supply of business development services facilitates the entire and on-time repayment of the loans. About 80 percent of loans have been regularly repaid.

²³ CLUSA initiated the provision of loans through GAPI

5.4 Centro de Aconselhamento para Desenvolvimento Industrial

CADI, advisory center for industrial development, is a partnership among the government (MIC), international organisations (UNIDO) and the private sector (AIMO - Industrial Association in Mozambique), which intends to reinforce business and investment development in Mozambique. The beneficiaries of CADI are emerging and already existing SMEs that are supported through training, consultancy and research services.

CADI has specialised counsellors in the following areas:

- Economics and finances
- Research and technology transfer
- Research, studies and market penetration strategies
- Studies and human resources capacity
- Project development cycle
- Training, consultancy and research (basic activities)

Currently, CADI in partnership with UNIDO is developing the IT BISNET information services. This latter is a project provided for facilitating information sharing for SMEs between Maputo and the provinces. The service is still not available.

5.5 Technoserve

TechnoServe is a US-base non-profit development organisation founded in 1968. It started to operate in Mozambique since November 1997 when it received a grant from USAID to provide assistance to the agribusiness sector. Miranda Caju, Unidade de Produção de Castanha de Cajú de Morrupula, MOCIT/Citrum and Optima (Manica Oil – sunflower oil processing in Chimoio) are some of the enterprises assisted by TechnoServe. Since 1997, TechnoServe/Mozambique targets a number of new and existing agribusinesses, resulting in the creation of new jobs and increased purchases of agricultural products.

The services offered by TechnoServe are:

- Market and industry research
- Business plan development
- Business evaluation
- Market and financial linkages
- Operational consulting and advice
- Managerial and employee training.

Furthermore, TechnoServe organises the Rural Enterprise Innovation Grant Programme (REIG) that awards US\$ 250,000 to Mozambican entrepreneurs in 2003. This programme is designed to support the creation of innovative and efficient productive lines that will create jobs and increase incomes in rural areas.

It also promotes financial management training programmes, such as Mozlink. This latter is a two-year programme designed to provide

Mozambican businessmen with tailored information about a productive and competitive management of their enterprises. This programme focuses on eight industries with significant potential growth: oilseed processing, cashew processing, business process outsourcing, wood products, eco-tourism, flowers and ornamentals, and garments.

5.6 Malonda Program

The Malonda²⁴ Programme intends *"to improve business environment, co-invest in strategic infrastructures or services in order to diminish risk and cut operational costs for investors and improve the local know-how"* (Business Plan Proposal, 2003-2006, pg. 3). It is an initiative between the Swedish International Development Authority (SIDA) and the Mozambican Government. It started in 2001 and operates mainly in the province of Niassa.

It targets only economically active people and has the objective to achieve self-sustainability within 2006. They established 15 consortiums and by the end of 2003 they estimate that 50 percent of the total costs will be covered. This programme intends to increase income in the province and develop the entrepreneurial capacity of private sector.

Their areas of work are:

- (i) strategic services to look at market failure
- (ii) business center
- (iii) legal services
- (iv) business information
- (v) microfinance in rural areas
- (vi) joint-ventures through less than one year contract in which they share both profits and losses
- (vii) outgrowing

The key-point of the Malonda Programme is to promote the private sector through investments in the form of risk capital and management support for contractual joint ventures.

5.7 Aid to Artisans

ATA (Aid To Artisans) is a programme that started working in Mozambique in 1998. It targets artisans and small and medium-sized enterprises and intends to develop local, regional and international markets for handcraft products among Mozambique, Tanzania and South Africa.

The founders for the Mozambique programme include Ford Foundation, Kellogg Foundation, West Foundation, PODE, Ewing Family Trust and other donors. ATA-Mozambique received a grant of USD 2.8 million from USAID.

²⁴ Malonda means business in the language spoken in Niassa.

ATA's main tasks include promoting micro enterprises support activities in three provinces, such as Maputo, Sofala and Nampula. It provides technical assistance in the form of business training, product development and marketing services.

The rationale lies in the intention of developing entrepreneurial skills of local producers so that they may generate and maintain sales beyond the life of the project.

5.8 MEDA

The mission of MEDA is to help poor people improve their lives through economic development. MEDA is attempting to reach the poorest by helping them to develop economic activities supported by the Canadian Development Agency, CIDA, but it recently received additional funds from Australian Aid and the USAID.

MEDA is at present financing a micro-project based on about 19 informal and formal markets of Maputo. For instance, the Xikelene market, one of Maputo's largest markets, serves as a Maputo center office for MEDA's credit officers, cashiers and clients.

The goal of the project is to sustain the market operators with the provision of small working capital loans. They should be spent on the purchase of merchandise or raw materials.

MEDA believes that expanding the activity base, incomes of the urban poor will increase. Furthermore, the programme aims at reaching and stimulating those entrepreneurs with skills and motivation necessary to develop their activities into competitive and remunerative firms.

The future challenges of MEDA will be:

- Expanding into surrounding suburban areas of Maputo city and introducing additional loan products as demanded by the clients. As well MEDA plans to continue its expansion in the Maputo province.
- Managing rapid expansion while reducing the portfolio at risk and training a solid core of Mozambican personnel to manage independently their economic business.

5.9 Fundo Fomento Pequena Industria (FFPI)

The Fundo Fomento Pequena Industria was initially managed by MIC, but it is now privatised and works like a commercial bank. It offers both credit and technical assistance to SMEs. In particular, it provides entrepreneurs with viability studies for small projects and monitoring after the loan is given. The applied interest rate is slightly below market rates (23%). FFPI gives credits up to \$60,000 and it has six small lines of credit: for SMEs in industry in Manica (SIDA - 2.5 billion meticaís), for industry moageira, small fishing activities in Nampula (IFAD/NORAD \$0.5 million), small fishing activities in Sofala (IFAD/NORAD \$1.3 million), rural trade (IFAD/NORAD \$0.6 million) and SMEs in industry and other sectors except agriculture (ADB \$1.2 million).

6. Conclusions

Small and medium sized companies meet a wide range of obstacles to their development. On the basis of what reported by those interviewed, we classify these constraints into four groups:

- credit market
- macroeconomic environment
- institutional framework
- infrastructures and market

In order to support SMEs, it is necessary to create appropriate strategies and policies that remove SMEs constraints, give direction, mobilise resources and build local capabilities for fostering entrepreneurial development. There is need for a government institution able to formulate a private sector development policy and coordinate all the initiatives in favour of SMEs.

New and dynamic financial institutions, such as GAPI, AMODER, SOCREMO, TechnoServe, show that it is possible to work with SMEs and transform them in a source of strength for the Mozambican economy. Therefore, we suggest that they are supported in their provision of financial and non-financial services to SMEs.

In the short term, two priority actions are suggested:

1. Establishing risk capital funds. Donors should define and mobilise resources necessary to introduce joint ventures as new investment methods for financing SMEs. This way of operating may have a positive effect on the growth of the private sector. Enterprises could share capacities and information and upgrade their business through new technologies and strategies.
2. Supporting technical assistance. SMEs are not able to make a business plan, manage its accounting (in the case they have one), develop their marketing (sometimes they are able to produce, but not to deliver their products) and take advantage of technological innovation. Lack of entrepreneurial attitude is an urgent problem, whose resolution is important for enabling SMEs to gain credibility in the bank system. Therefore, we recognise that specialised consultancy and technical and vocational training are a priority for SME development.

Business associations might be a valuable channel through which spread information about technology, market opportunities, international quality standards, laws and other legal procedures. However, they also need capacity building in order to assist efficiently SMEs.

In the long term, it is essential to work on the macroeconomic reforms and build institutional capacity to foster the private sector in Mozambique. Regarding the financial sector reform, there is strong demand for strengthening banking supervision and transparent funding mechanisms.

We suggest that the Italian Cooperation provides a comprehensive package of support that includes not only credit but also technical assistance in terms of technology, production, market strategy and information.

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APPENDIX I

DEVELOPMENT CREDIT INSTITUTIONS

Apart from the commercial banks, the banking legislation entitles other institutions to offer exclusively credit, while saving facilities are prohibited. They are usually characterised by dependency on donors' funds, limited outreach, scarce internal capacity and lack of accumulated capital. Furthermore, there is a wide range of initiatives that target SMEs and offer both lending and business development services. Below we make a list of the main institutions. A more detailed list is provided by IFAD working paper entitled by "Financial Support to Market Linkage Operations" (please see bibliografy).

GAPI (Gabinete de promoção para Pequena Indústria)

GAPI was established in 1990 to finance and support the SMEs and it was registered as financial company owned by Friedrich Ebert Foundation and the Ministry of Planning and Finance. It provides loans to more than 200 smallholder associations, consultancy and business services. GAPI's funds are grants and loans from the German KfW, the French CFD, DANIDA, Nordic Development Fund and USAID. GAPI was selected as a potentially partner to issue credit to rural traders under the IFAD-finance programme. It has a portfolio of about 13 million USD and its average credit is about 35, 000 USD and is willing to expand but is constrained by available financial resources and institutional capacities (Iacovone et al., 2003).

AMODER (Associação Moçambicana para o Desenvolvimento Rural)

AMODER is a development financing institution established in 1993 to provide rural financial services mainly to projects on commercialisation of agricultural goods (75 percent of the loans are given to rural traders). Recently AMODER is trying to diversify its loan portfolio according to the donors' requirements by investing on other sectors, such as fisheries, rural transport and small industry. It operates in six provinces and issues about 200 loans per year with an interest rate that varies between 3 and 5 percent per month. Medium to long-term loans for housing rehabilitation have 2,25 percent interest rate per month. The financial support to AMODER comes from the European Union, DANIDA, Irish Aid, Sida and Oxfam (Belgium).

FFPI (Fundo de Fomento para Pequena Indústria)

FFPI is a Government owned development fund that operates since 1994. Originally it was capitalised with funding from SIDA (Swedish International Development Agency). The Board of Directors includes representatives from both the public sector (MPF, MIC, BoM) and the private sector. FFPI provides financial and business development services for small entrepreneurs its portfolio account for about 200 loans per year. The effective interest rate is about 32 percent per year. They have four offices in the country: Maputo, Nampula, Manica and Niassa.

SOCREMO (Sociedade de Crédito de Moçambique)

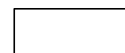
SOCREMO, established in 1998 and owned by the Ministry of Labour, GAPI, LFS (a German consulting company), the Agricultural Union of Cooperatives (UGC) and the Christian Council of Mozambique, provides financial services to micro-

entrepreneurs. Loans amount can start from US\$ 20-50 to US\$ 5000. SOCREMO has three branches: two in Maputo and one in Beira.

FCC (Fundo Comunitário de Crédito)

FCC is a Mozambican microfinance institution subsidised by World Relief. It operates all over the country. There are seven branches in the Southern provinces of Maputo, Gaza and Inhambane and three in the Northern branches of Nampula and Niassa. It reaches about 7000 clients, mostly traders, in both peri-urban and rural areas. FCC works mainly through community banks, although it is starting new products, including loans to individual clients and micro leasing. The perspective is to expand their coverage and reach 26000 clients in September 2006.

APPENDIX II



QUESTIONNAIRE FOR SMALL AND MEDIUM ENTERPRISES

Note: The Italian Cooperation is implementing a project on small and medium enterprise development in Mozambique. More precisely, it targets economic activities affected by the flood in 2000. The project wants to broaden the provision of credit to SMEs, in particular in rural areas. Therefore, we would like to ask you what the main constraints faced by your company are, particularly in terms of access to financial resources, and how you try to overcome them.

We highly appreciate your time and collaboration!

1. In which sector do you operate?
 - a) Agriculture
 - b) Agro-industry
 - c) Industry
 - d) Transport
 - e) Trade
 - f) Tourism
 - g) Others_____

2. Have you ever applied for a loan?
 - Yes and I got it (specify how many times).
 - No and I am not interested in it.
 - Why?
 - Had own capital
 - Too expensive credit cost
 - No sufficient collaterals
 - Too short repayment period
 - The scale of activities is small
 - High risk activity
 - Other reasons (e.g.: lack of accounting system and business plan, difficulties in registering the business)
 - Lack of capacity to manage the amount of credit
 - Yes but I did not get it
 - Why?
 - The bank said that the risk of investment was too high
 - Lack of collaterals
 - The profitability of the investment was low and it could not be able to sustain the debt services
 - Other reasons (e.g.: lack of accounting system and business plan, difficulties in registering the business)

3. Do you think that low access to credit is an important constraint for your business?
 - **Yes**
 - **No**

4. Which other constraints do you face?
 - Infrastructures
 - Collaterals
 - Entrepreneurial capacities
 - _____

5. What do you need a credit for?
 - Regular expenditures of the company
 - Products commercialisation
 - To buy inputs
 - Investment:
 - Machinery
 - Infrastructures

- Expansion and modernisation the company
 - Training of human resources
 - Others_____
6. In the case of need for a credit, where do you ask for it? (Identify the institution):
- Financial institutions (specify)

 - Non financial institutions (specify)

 - Informal sources (friends/relatives)
 - Own funds
 - Others_____
7. Which are the main requirements required by financial institutions in order to get their credit?
- Collaterals
 - Low risk
 - Type of sector
 - Personal contacts
 - Other relevant factors (specify)

8. Are you interested in getting more credit at the current interest rate level?
- **Yes**
 - **No**
9. If **Yes**, how much credit do you need to finance your business?

10. In which way limited or inexistent access of credit has a negative impact on your economic activity?
- Less productivity and competitiveness
 - Scarce investment on technology and human resources development
 - Not efficient use of the available capacities
 - Impediment to explore economy of scale
 - Other
11. Are there effective initiatives to increase access to credit for SMEs?
- **Yes (specify)**

 - **No**
12. If yes, how would you improve their performance?

13. If **no**, what do you suggest that Government, donors, banks should do in order to foster SME development?

14. In addition to credit, what other facilities does your enterprise need?
- Technical assistance
 - Savings
 - Insurance
15. What do you think Government, donors, Bank of Mozambique should do in order to improve financial institutions supply for SMEs?

APPENDIX III

Main results from our questionnaires²⁵

1. In which sector do you operate?

Sector	Agriculture	Commerce	Transport	Other
Number of companies	6	17	4	7

2. Have you ever applied for a loan?

Loans	Yes	No
Number of companies	16	15

3. Do you think that low access to credit is an important constraint for your business?

Loan as a constraint	Yes	No
Number of companies	28	3

4. Which other constraints do you face?

Other constraints	Infrastructure	Collateral	Entrepreneurial capacity	Other
Number of companies	8	4	7	12

5. What do you need a credit for?

Need for credit	Investment	Commercialisation	Sale of inputs	Other
Number of company	24	11	7	7

6. In the case of need for a credit, where do you ask for it?

Sources of credit	Financial Institutions	Non Financial Institutions	Informal sources	Own capital	Other
Number of company	18	0	3	10	2

7. Which are the main requirements required by financial institutions in order to get their credit?

Requirements of financial institutions	Collateral	Low risk	Type of sector	Personal contacts	Other
Number of companies	16	5	2	10	6

8. Are you interested in getting more credit at the current interest rate level?

More credit	Yes	No
Number of companies	3	26

9. In which way limited or inexistent access of credit has a negative impact on your economic activity?

Negative effects of lack of credit	Less productivity and competitiveness	Scarce investment on technology and human resources development	Not efficient use of the available capacities	Impediment to explore economy of scale	Other
Number of companies	14	12	5	9	7

10. In addition to credit, what other facilities does your enterprise need?

Other Needed Facilities	Technical Assistance	Savings	Insurance	Other
Number of companies	20	8	5	8

²⁵ To sum up, we interviewed 32 enterprises in 4 provinces: Maputo, Inhambane, Gaza and Sofala. Some questions could have more than one answer.

APPENDIX IV:

Maputo

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Elias Come, CADI/AIMO
Prosperino Galipoli, UGC
Ismael Ossemane, UNAC
James Rudolph Lafleur, CTA
Monika Branks, Verde Azul Consulting
Trudy Schwarz, MMF - MEDA
Ia Patterson, AMODER
Fidelx Kulipossa, GAPI
António Gracio, Director Comercial BCI
Jack Walker, Technoserve
Arlindo Matavele, Enterprise Mozambique
Gilberto Barros, World Bank (PODE-CAT)
Steven Dils, UNIDO
Custódio Mucavele, IFAD
Carsten Sandhop, KfW
Xavier Cirera, MIC
Eugénio Simão, ASSEMA
Philip Tonks, USAID
Elsa Mapilele, USAID
Samuel Chissico, AGRARIUS
Joaquina Maria, DPIC – Província
Tiago Chauque, DPIC – Província
Armando Lifaniça, DPIC – Província
Armindo Braz Barradas, DPIC – Cidade
Eusébia Xavier, DPIC – Província
Gustavo Miranda, GAPI
Simão Sevene, AJAM
Fernando Salomão Mussane, AJAM
Sarmiento Saul, AJAM

Maputo province (enterprises)

1. Padaria e Pastelaria Cristal

Bairro Jorge Dimitrov, Tel. 01 470210
Contact: Sr Ibrahim (gerente/sócio)

2. Riplex – Indústria de Embalagens Plásticas

Avenida de Moçambique n. 1548
Tel./Fax: +258 1 475054 Cell: 082 301010
Rangendra Dhirauglal

3. Casa de Carimbos, Rua da Mesquita
Sr Abrão

4. Cantina Magaia

Av Moçambique, em frente da Riplex
Silvino Castigo Magaia

5. Quiosque Baltazar

Salomão Samuel
Tel. 01 477531. cell 082 413 000

6. Njingiritane

Avenida 25 de Setembro
Carlos Alberto. Cell 082 482 035

7. Kilimanjaro

Avenida 25 de Setembro
Sr Chico

8. Tabacaria Paris

Avenida 25 de Setembro
Contact: sr. Dipack
Cell: 082 727105

9. Supermercado UNIMOZ

Contact: Cremilda Maganlal
082 300 598

10. Agro-Pecuária de Mohalaze, Matola

Contact: Manuel Augusto Pessane
Cell: 082 81 80 57, Bairro do Zimpeto, Q. 12, Maputo

11. Agro-Pecuária de Sarmento Saúl & Fernando Salomão Mussane

Bairro Zona Verde, Av. 4 de Outubro-Matola
Contactos: Sarmento Saúl – Tel: 01 47 69 26, Maputo
Fernando Salomão Mussane – Tel: 01 47 53 34, Maputo

12. Agro-Pecuária, Intaca. Congolote

Contacts: Bento Firmino Nhamuave & Simão Sevene, Bairro do Zimpeto,
Simão Sevene, Cel: 082 71 89 66, Casa, Tel: 47 22 98, Maputo

13. Agro-Pecuária, Macia - Gaza

Contact: André Eugénio Muchanga
Cel: 082 88 47 47, 082 31 40 51

14. Quinta Agro-Pecuária Gouveia, Zimpeto

Contact: Gouveia, Bairro do Zimpeto, Maputo
Simão Sevene, Cel: 082 71 89 66, Tel: 47 22 98

Sofala (enterprises)**1. ACIS – Associação Comercial e Industrial de Sofala**

Casa Infante de Sagres, C.P. 07.Beira, Moçambique.
Ph/fax (258) 3 320335
Carrie Davies (Director-Links Consulting Lda)
Executive secretary
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2. Union Transport

P.O Box. 1682, Beira, Moçambique
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3. Moura Correia e Aragao

Tel. 03 323587
Moura Correia & Aragao (Beira), Lda
Adolfo Mahomed Siddiq Mahomed (sócio-gerente)

4. SCA Consultores – Sociedade de Consultoria e Auditoria & Serviços, Lda

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Tel (258-3) 323019 Fax (258-3) 323021
Roberto Filimone (sócio-gerente)
sca.beira@teledata.mz

5. ASTROS – Associação dos Transportadores Rodoviários de Sofala

Rua Duarte da Costa, 65. C.Postal 1438
Tel: 03 353465/67
Fax: 03 328612
Contact: Joaquim Mesquita

6. FIELD TECH SALES (MOÇ), LDA

Chris Myers (General Manager), Avenida Base N'Tchinga, Munhava Beira,
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mailto:chris.field@teledata.mz

7. ACB – Associação Comercial da Beira

Zaide Mohamed Aly (president),
Gabriel de Oliveira (1st vice-president)
Eugénio Caetano (executive secretary)
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8. Beira Manpower Management Limited

Faruk Ibrahim (sócio-gerente)
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9. Direcção Provincial de Indústria e Comércio

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10. Centro de Promoção de Investimentos

Anastásio Miguel Ndapassoa (jurista)
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11. GTZ – REDE Promoção Regional de Economia

Ninho de Empresas da Beira
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12. Transportes Carlos Mesquita

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13. Cooperação Austríaca

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Inhambane (enterprises)

1. Pastelaria Moçambicana

Avenida Eduardo Mondlane
Aligy Dauto Aligy (gerente)
Chaharzade A. Reman Mussagy (proprietária)

2. Tswuanene Comercial

Catarina da Luz Aleluia e Guilherme Aleluia (cell: 082 826403)
Tel. 023 20111

3. Direcção Provincial de Indústria e Comércio

Américo De Jenga (Director , cell: 082 501992)
Artur Joaquim (Chefe de Departamento de Indústria)
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4. Empresa Moderna (Tipografia e Encadernação)

Avenida Acordos de Lusaka
Faizal Momade Bay
Tel. 023 20534

5. Direcção Provincial de Agricultura e Desenvolvimento Rural

Sr Limbawe
Cell: 082 482368

6. Associação de Agentes Económicos da Provincia de Inhambane (AAEPI)

Construções Vuxa

Felizardo Vaz (Presidente)

Cell: 082 318528

7. Loja de Negócios de Inhambane

Fernando Henriques

Almeida José Almeida

Tel. 023 20806/20814

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8. Copromol – Mozambique Coconut Products, Ltd

Faruk Agige (General Manager)

Estrada Nacional n.1

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Maxixe, Mozambique

Gaza, Chokwe (enterprises)

1. Organizações Cassamo Dauto Rugunate

Avenida Eduardo Mondlane

Proprietário: Cassamo Dauto Rugunate

Tel. 021 20023, cell: 082 707 711

2. Agro-Comercial Dimas

Proprietário: Daniel Jaime Dimas

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3. António Manuel da Encarnação Rodrigues

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Cell: 082 654 417, 082 414 881

4. CESAGRO

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7. Hotel Limpopo

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