

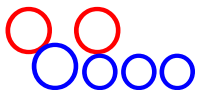
# CAPSA

## Capacitating Sector Analyses

A practical training methodology to analyse value chains.

### **Training Manual for the participants**

**Draft version  
14<sup>th</sup> May 04  
for comments**



**Hans Posthumus Consultancy**

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**Hans Posthumus**

[hans@hposthumus.nl](mailto:hans@hposthumus.nl)      [www.hposthumus.nl](http://www.hposthumus.nl)  
Prof. van de Veldenstraat 8, 5427 ST Boekel, The Netherlands  
Tel: +31(0)492-329458 - Fax +31(0)492-840422 - Cell 06-16516 453

# Preface

## **Building capacity**

CAPSA combines *Capacitating (CAP)* and *Sub sector Analyses (SA)*. On the one hand CAPSA provides a methodology and instruments for participants to undertake a sub sector analysis, on the other hand, participants are being trained in general aspects of small enterprise development: two different yet complementary objectives.

A thorough *Sub Sector Analyses*, or *Value Chain Analyses* as they are sometimes referred to, results in a complete picture of the sub sector; how it functions, what the bottlenecks are and what opportunities the sub sector holds. Thereafter, CAPSA assists in designing appropriate interventions that improve the functioning of the actors within that sub sector.

Sub sector analyses are complicated and thus often undertaken by (international) experts. CAPSA however trains and guides people with limited experience to undertake such an exercise. This greatly improves their ownership of the analysis and the implementation of the resulting intervention. It avoids possible loss of information and continuity that might occur when outside experts analyse a sub sector whereafter local actors implement the resulting intervention. Naturally, the duration of the exercise is longer than when done by experts, but the objectives and results are two-fold: a sub sector analysis concluded and participants capacitated.

## **Targeting**

CAPSA is meant for a rather broad public but participants must have at least one thing in common: an interest and a desire to learn more about local economic development. They can come from organisations such as NGOs that are active with *Private Sector Development*, but they might also come from business associations or other sector based actors. The potential candidates do not have to be experienced economists: in many cases they will be programme staff with a variety of backgrounds and as long as they are professionals in their fields, they will be able to participate in this course. Experience in certain fields such as participatory analyses will ease participation, just like an economic or business background will improve results.

## **Process**

Sometimes the participating organisations are already active in certain sub sectors. In that case CAPSA can contribute in a thorough analysis of the sub sector and assist in the design or improvement of existing interventions. However, the latter will depend on the potentiality of the sub sector and as such CAPSA may contribute to a strategic reorientation of the organisations towards other sub sectors.

In other cases the participating organisations are not limited to certain sub sectors and in that case CAPSA must be preceded by another exercise called *Economic Mapping*: an overall picture is made of all the sub sectors and by applying certain criteria and tools, one or two promising sub sectors are identified. CAPSA does not deal with this economic mapping itself even though attention is paid to the reasoning and the criteria for the sub sector selection.

## Contents

The training course starts with an introductory session explaining the *entrepreneurial principles* and the *sub sector concepts and classifications*, using cases, self-learning and group work, both in the classroom as well as in the field. Its resulting fieldwork will ensure a demarcation of the sub sector and a first introduction of the team into the sub sector analysis.

The second unit deals with the *basic business principles* with a focus on market orientation, segmentation and general business strategy development. A supportive module provides the participants with *interview techniques* to enable them to select, prepare and interview the entrepreneurs.

The third unit introduces *the mapping principles* and includes exercises to enable the team to draw basic sub sector maps. It contains a sub unit on the *identification of sources* of information, primary and secondary information from entrepreneurs, their suppliers, consumers and key informants. This will result in an action plan with checklists for collecting sufficient information to improve the basic sub sector map. A supportive module on *database design* and maintenance will assist them in the analysis of the fieldwork results.

The fourth unit guides the team in *analysing profit margins* in the various channels where after they are able to analyse the economic performance, including trends and dynamics of the sub sector. This information will be used to develop the 'final sub sector map' with, whenever possible, over layers of economic indicators that will form the basis for the analysis. The *SWOT analysis* is explained and practiced. Suggestions for both economical and organisational selection criteria are provided that will be discussed in feedback sessions with the entrepreneurs and key actors.

The fifth unit deals with the importance and methodology of undertaking an *organisational landscaping* exercise and introduces the basic concepts of Business Development Services. Thereafter the team will be able to identify bottlenecks in service provision and possible intervention areas, undertake the landscaping exercise and make an organisational gap-analysis.

In the sixth unit, the participants are guided on the design process using *scenarios and other selection instruments* to select and design the appropriate intervention strategy. The supportive unit on the *Logical Framework Approach* will assist them in the design of a concrete intervention proposal.

## Approach

Ideally a study team is created with participants from various organisations. This will increase cross-coordination between organisations, form a broader basis for implementation of possibly resulting intervention proposals and last but not least, increase the efficiency of this capacity building tool. A training needs assessment shall form the basis for CAPSAs training cycle that needs to be adjusted to the expertise and needs of the team.

A balance needs to be found between the necessary time to analyse the sub sector, maintaining the interest of the team members and the available resources of the participating organisations. Each step would start with a short training, where after the team will execute another part of the field study. There are six training intervals and if the team members spent some 2-3 days per week for field work the entire study will consume some 25 weeks.

However, the manual is designed in a modular way and can thus be applied in a flexible manner. If the focus is on capacitating the participants, the complete course can be reduced to some 2 weeks of 'practical theory'. Moreover, the training needs assessment will provide information on which modules are relevant or not, thus enabling the trainer to provide a tailor made course.

## CAPSA

The training should be done by a trainer/economist who is experienced in undertaking sub sector analyses. Although the trainer would ideally be involved in the entire sub sector analysis, alternatives can be sought for the field work in case (s)he is not available for which reference is made to the Angola case description hereafter.

CAPSA comprises of two manuals: one for the participants and one for the trainer. In the latter session overviews, didactical notes and answers to the exercises are included.

Hereafter the case description of CAPSA in Angola is presented, providing more insight into the methodology, as well as a systematic overview of the course and some examples of training cycles.

# CAPSA in ANGOLA

## Introduction

From mid 2001 to mid 2002 a joint sub sector analysis was undertaken in Lubango, Angola. The author, hereafter referred to as the external consultant, together with the regional SNV PSD consultant, trained and guided local NGOs to undertake an economic mapping and sub sector analysis. The exercise was initiated and co-financed by SNV Angola. After the entire exercise had been completed, the author was requested to undertake a context analysis and economic mapping in three provinces to prepare the ground for three more sub sector analyses. In order to enable SNV to train and guide these new teams to study these sub sectors, the author was requested to prepare a training manual. This CAPSA training manual is the result of that exercise.

## Brief description

In Angola, only now emerging from an armed conflict, there are only a few NGOs and most NGOs are oriented towards emergency aid with little or no experience in PSD/SED issues. SNV supported three NGOs to analyse the productive sector in urban and peri-urban Lubango. A study team was formed and on-the-job training provided to the NGO staff. First an economic mapping was made to identify existing and potential sub-sectors. The NGOs chose three sub-sectors that appeared to have potential and need for further development. A sub-sector analysis was applied and project interventions were subsequently elaborated.

## Context

SNV had signed partnership agreements with two major local NGOs to advise and assist them in general strategic and operational issues. These NGOs were to some extent involved in SED through some of their projects. However, it was felt that these projects were not very successful. This was partly due to Angola being torn apart by internal conflicts with most NGOs focusing on the most vulnerable people through emergency programmes. However, it was also agreed that there was too little in-depth knowledge of the productive sectors and that many project proposals missed a profound analysis and thus did not always address the constraints in the most appropriate way.

SNV offered to train the two NGOs in how to analyse the productive sector in order to design effective interventions. Two other interested NGOs were invited to participate as well and a study team of 9 members (two of each NGO and one junior from SNV) was formed. The team members were to spend two days a week on the study during a six-month period and the NGOs were to cover the operational costs<sup>1</sup>. SNV hired two consultants that would define an appropriate methodology, train the team members at various intervals, provide backstopping during the study and assist the team in the analysis and design of the interventions proposals, as well as to develop a capacity building plan for the participating NGOs.

## Objectives

The objectives of the NGOs were to analyse the productive sectors in urban and peri-urban Lubango, after which interventions would be designed and implemented by these NGOs to improve the performance of small enterprises in certain sub-sectors. The NGOs formulated a list of 15 objectives,

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<sup>1</sup> One NGO dropped out almost immediately and the team continued with 6 members.

which were all related to the main objective, but maybe due to their limited knowledge in this field, these were a mixture of objectives and activities and were not very specifically defined.

The objective of SNV was not only to assist the NGOs in this exercise but also to build capacity on general SED issues within these NGOs. Therefore SNV had formulated the immediate objectives of this exercise as follows:

- Develop an appropriate methodology, instruments and tools
- Enable the NGOs to apply the instruments and tools of that methodology
- Draw up three intervention proposals
- Complete an organisational analysis and capacity building plan for the NGOs

## **Description of the main activities and the roles of the different actors**

### *Methodology*

The **Sub-Sector Analysis (SSA)** offers a framework for evaluating enterprise performance per sub-sector and ideally results in effective and efficient interventions. A sub-sector is defined through the basic raw material that is being used for the production, transformation and distribution i.e. the entire chain from supplier to end consumer. By analysing the functioning of each actor in the chain, including cross-linkages, competition and coordination, in-depth knowledge is obtained on each type of enterprise. Bottlenecks and opportunities are identified and, by applying the leverage principle, interventions can be designed that are effective, cost-efficient and have a great impact on the chosen category of enterprises (in this case micro- and small producers).

Before the SSA can be applied to potential sub-sectors, a general **Economic Mapping (EM)** needs to be carried out to determine which sub-sectors are present in the local economy and which of these show most potential for (further) development. An inventory of all sub-sectors is made and additional information from both primary (the enterprises) and secondary sources (key informants, institutions, etc.) for all the sub-sectors is collected. After that a SWOT-analysis can be made for each sub-sector and the defined selection criteria can be applied. These criteria are partly economic (added value, employment creation, export potential, etc.) and are partly related to the objectives of the participating organisations (gender, location, sector related, etc.).

Once the sub-sectors have been defined, the SSA starts with more in-depth information being collected on all the relevant aspects. During the process of collecting the relevant information a first draft of the sub-sector map is drawn. Most information is obtained from the primary sources but the research is not limited to the chosen target group but includes all actors in the chain, from micro- to large enterprises and from suppliers to end users. Simplified profit calculations and consumer surveys are the major instruments in use. Gaps in the map require more research and more research information will change the map again: an iterative process until certainty is obtained about the correctness of the map. The correctness of the map is confirmed in feedback sessions with entrepreneurs and other actors in the sub-sector.

Major constraints and opportunities almost automatically emerge from the drawn sub-sector map. An institutional landscaping will provide information on relevant institutions and their activities for the sub-sector. Not only will that landscaping avoid duplicating or conflicting interventions, it will also provide opportunities for coordination and cooperation. After that interventions are designed that can range from advocacy through market linkages to credit.

### *The process*

August 2001

The study was initiated with a three-day workshop where the external consultants met with the SNV staff and a few key representatives of the NGOs. The principles of the methodology were



explained and discussed and through a participative approach a detailed operational plan was drawn up by the participants.

September 2001

*Soon after that, a one-week training session was held on various introductory issues such as entrepreneurship and small enterprise development aspects. Ample time was spent elaborating questionnaires and interviewing entrepreneurs in the field, after which a first draft map of various sub-sectors was made. Simultaneously, secondary sources were identified to obtain macro-economic information and the training programme concluded with a one-day workshop with the team and their directors, in which the sub-sector criteria were defined and a detailed planning agreed upon.*

The team continued interviewing a considerable number of entrepreneurs and key informants in various sub sectors as well as consulting various secondary sources during two months. They presented profiles for each sub-sector, describing the positive and negative elements, and through various working sessions this process was finalised. Their findings were presented to their directors and both economic and organisational criteria were applied. It was agreed that three of the ten identified sub-sectors had some need and potential for development.

December 2001

A second one-week training took place, in which additional instruments such as the simplified profit analysis, participatory budgeting and consumer research were explained and practised. After that the sub-sector maps were further elaborated for the three identified sub-sectors and the training concluded with a detailed planning for the next phase.

The team completed the initiated exercises and maps in the months thereafter and organised a feedback workshop with entrepreneurs and various stakeholders. Their findings were presented and discussed, making use of clarifying pictures and drawings, as well as supporting documents. Working sessions were held, after which the stakeholders confirmed the major findings and conclusions of the team.

March 2002

The consultants were invited for the last phase of drawing major conclusions, elaborating interventions and assessing the needs of the organisations. During the initial sessions it proved necessary to collect and verify more information and due to time constraints the organisational aspects had to be postponed. The analysis however led to three project proposals that were jointly elaborated and a draft proposal was written by the consultant. The NGOs later elaborated final project proposals.

### *Case specific considerations*

The applied methodology was based upon the SSA initially developed by Gemini<sup>2</sup> and later adapted by FAIDA<sup>3</sup>. However, the research is usually done by “experts” while in this specific case the actual research was done by the NGO staff. Although a certain familiarity with research and some economic insight is required, they are not “professionals” in the methodology. Therefore the analysis takes more time, but it does improve ownership of the process and the resulting interventions. The results of the applied methodology are thus not only the defined interventions as such, but new and applied knowledge for the team members in the specific sub-sectors and small enterprise development in general. The fact that various organisations researched the sub-sectors together, led to further cooperation and sharing of experiences between the organisations and their interventions.

### **Achievements and results**

<sup>2</sup> GEMINI Growth and Equity through Micro Enterprises and Institutions

<sup>3</sup> FAIDA Finance and Advice In Development Assistance for Small Enterprise Promotion

The study has taken some nine months altogether, fifty percent more than planned, and the fact that the team members have maintained their team spirit during the entire study period is an achievement in itself. The cooperation between the team members and their organisations continues even though the study has formally ended. The team members learned a lot. They have gained insight in general aspects of SED and of course the applied methodology. Last but not least, they feel they are owners of the proposed projects.

The direct and concrete results of the study are the three draft project proposals that most likely will be financed and implemented. All three projects include a market-monitoring element to measure impact and steer the project activities, while one project includes more research elements to obtain more in-depth information. The project set-up differs from other “action-delivery” projects in the region and they may be seen as pilot projects.

For SNV the exercise proved a starting point to draw up a strategy and capacity building plan for local organisations and institutions in the field of SED.

## **Follow-up**

### *NGO interventions*

In April 2002 the three projects were further elaborated by the three NGOs with the assistance of SNV and submitted to various donors. To date three donors (UNDP, USAID and Shell) have indicated an interest in financing all three projects. However, the three project proposals are now part of a larger programme that will assist the NGOs to enhance their capacity to deliver effective BDS to MSEs. The three pilots are thus practical instruments in this capacity building process, whereby it is envisaged that at the end of the 30 months project period the three organisations will have integrated BDS as a service component in their organisation. The project is in the form of a partnership between the three NGOs and SNV, in which each NGO is responsible for one intervention, but regular sharing of experience and joint learning is equally important. SNV will play a key role in training and capacity development of the three partners.

### *SNV PSD programme*

In May 2002 the needs and possibilities to implement a similar programme in three provinces were studied by the consultant. Potential SNV clients and promising sub-sectors were identified and characterised, after which a draft implementation plan, including key success factors and risk management strategies, was drawn up. A training manual has been developed by the author to enable the SNV/PSD officer to train more NGOs in the methodology, taking into account the learned lessons from the previous exercise.

The exercise also assisted SNV to develop a long-term strategy for improved support to micro- and small enterprises. One component will focus on capacitating local organizations that want to assist emerging micro producers through various instruments such as subsistence systems analyses, savings mobilisation, market information and diversification. The other component will focus on capacitating local organisations that want to develop BDS for MSEs, including micro-enterprise management, marketing and access to finance, basically following the logic of the previous (and now improved) exercise.

## Lessons learned, conclusions and recommendations

### *The process*

Although all participants were aware of the difficulty of applying the methodology in this NGO set-up, the entire process may have been underestimated.

More specific training at shorter intervals combined with continuous backstopping in-between these sessions would have improved the desired result. The foreseen backstopping by SNV was less than foreseen since this had to be done (part-time) by the SNV Director due to the vacant position of a PSD programme officer. The team made little use of the available backstopping by the external consultant. That might again be due to the perception the team may have had about the role of the external consultants, combined with the team's unfamiliarity in formulating "assistance needs". The latter might have been due to insufficient clarity of the team on the steps of the process.

Therefore the process should have been structured in more but shorter steps, each concluded with a go/no-go decision. Not only would this have given clarity to the team, but it would also have ensured that the information and findings of the previous step would have been completed satisfactorily, since the following steps are based upon the findings of these previous steps.

The impression remains that the team members to a certain extent lacked the analytical skills or attitude to apply the methodology. This is only natural and could have been resolved by more frequent sessions where they would be triggered to reply to questions. The step from analysis to interventions, which in this process is perceived as a big step, becomes more logical and sequential.

The process has taken a rather long time and team members were only available part-time. Although the allocated time was sufficient, members had to continue with other office tasks. That implies that members could not always participate on the planned days due to unforeseen or urgent tasks, which hampered the progress<sup>4</sup>. The team had limited experience or skills in writing papers and much time was spent on 'elaborating conclusions, resumes and presentations', which delayed the process and reduced the quality of the output

The process has led to an increased ownership by the NGOs of the projects and has provided them with knowledge about the sub-sector and general business development aspects. The gap that often exists between "external expert project elaboration" and the implementation of the projects is therefore reduced. Moreover, the costs of the entire SSA, including the limited use of these external consultants, is probably less than an SSA by external consultants, even though one might argue that the quality of the SSA may differ.

### *The methodology*

The EM proved to be rather difficult. In Angola, as in many other developing countries, little specific and up-to-date information is available, while the team also had problems to interpret macro-economic figures. The inventory of the present sub-sectors, and analysing their potential, has therefore absorbed considerable time and energy. On the other hand, certain sub-sectors were 'discovered' that were otherwise not likely to be considered.

The NGOs did not have a special relationship or track record with the enterprises in the chosen sub-sectors. It has therefore proven difficult for them to understand the sub-sectors and to gain trust from the enterprises to provide them with inside information. Moreover, many NGOs were perceived as 'delivering emergency aid' organisations.

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<sup>4</sup> Some members were true volunteers and received little if any remuneration from their organisations.

The NGOs had chosen to support micro- and small producers in three sub-sectors. Given the extreme limited productive sector in the region, the number of actors, i.e. the potential target group or clients, is simply limited. As a result, the cost-benefit ratio of the elaborated interventions is rather high. Hence, these projects should also be seen as pilot projects, in which capacity building of NGOs to design and manage such projects is equally important. Given the rather embryonic stage of these NGOs, this seems justifiable.

Although the SSA should lead to interventions, in which the leverage effect creates a major impact, no direct leverage was identified in these SSAs. Most of the interventions were related to market linkages and included components to improve access to markets, improve company operations (technical and managerial training) and monitoring of market developments. The training and research components make these interventions rather expensive, but given the similarity between the three project proposals some additional gain may be realised. Moreover, the initial investments are rather high due to the development of training material and setting up of systems, but the cost-benefit ratio will improve with more future clients.

### *Applied lessons learned*

The proposed process has taken into account these lessons learned.

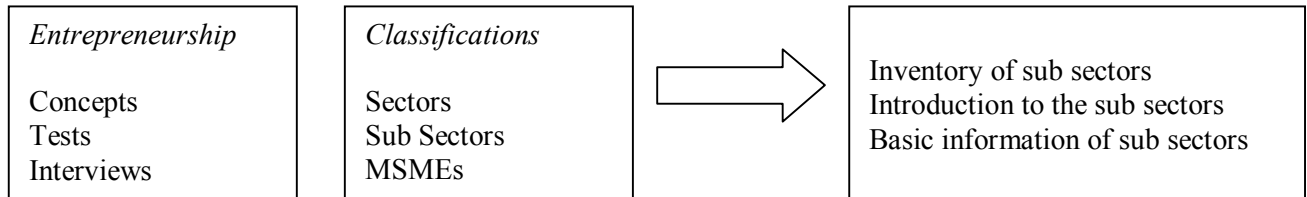
The recruited PSD programme officer will spend 50% of his time on the planned SSAs and a training manual has been prepared to provide the participants with more business and enterprise development theory and practises, exercises and case studies. Six training moments of each 2-3 days are planned with assignments and feedback sessions in-between. In that way the participants are coached during the entire six-month process.

Moreover, it was realised that NGOs without a relationship with the perceived target group and without a track record in PSD/SED face a lot of difficulties applying the process (see also 6). Therefore it is advisable to either work with NGOs that do have a relationship with certain target groups (i.e. they are active in the sub-sector) or to work with NGOs that are experienced in PSD/SED programmes in general.

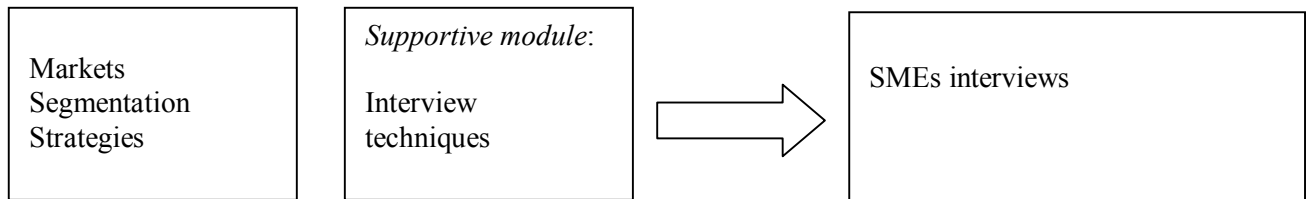
When working with the first type of NGOs, which is the majority of the Angolan NGOs, the Economic Mapping should preferably be done by experts, including a first analysis of the sub-sectors. The combination of a promising sub-sector with NGOs that are active in that sub-sector appears ideal for this approach. Other organisations like sector-specific associations can and should be included as partners. NGOs with some experience in PSD/SED may in principle be suitable for an Economic Mapping exercise, albeit -depending on their expertise- with certain external expert assistance.

# Overview of steps and training units

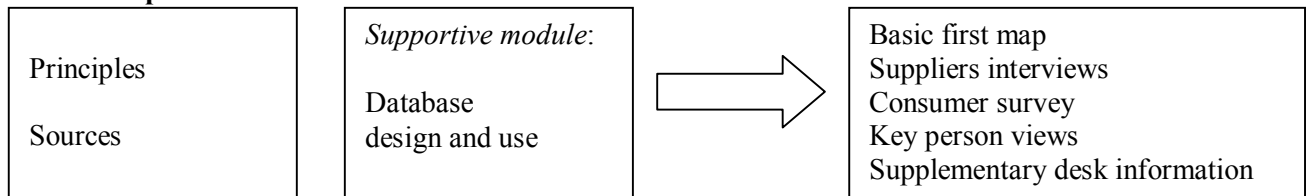
## 1 Context



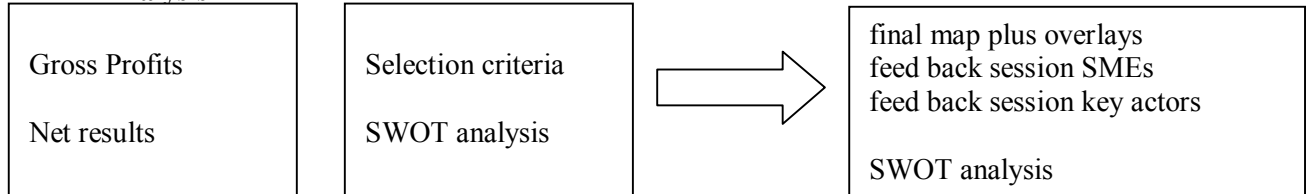
## 2 Business



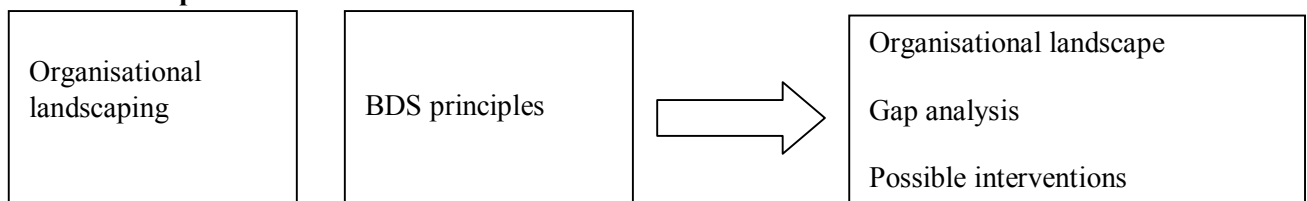
## 3 Maps



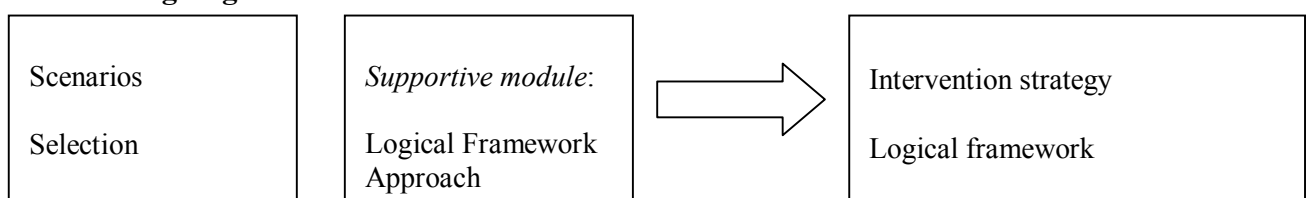
## 4 Analysis



## 5 Principles



## 6 Designing



# Examples of training cycles

**Steady: 25 weeks**

Weeks:	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24	25
<b>unit 1</b>	█																								
Fieldwork		█																							
<b>unit 2</b>			█																						
Fieldwork				█	█	█	█																		
<b>unit 3</b>							█																		
Fieldwork								█	█	█	█														
<b>unit 4</b>											█														
Fieldwork												█	█	█	█	█									
<b>unit 5</b>																	█								
Fieldwork																		█	█	█	█				
<b>unit 6</b>																						█			
Fieldwork																							█	█	█
<b>evaluation</b>																									█

**Rapid: 20 weeks**

Weeks:	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20					
<b>unit 1</b>	█																								
Fieldwork		█																							
<b>unit 2</b>			█																						
Fieldwork				█	█																				
<b>unit 3</b>					█																				
Fieldwork						█	█	█	█																
<b>unit 4</b>									█																
Fieldwork										█	█	█	█												
<b>unit 5</b>													█												
Fieldwork														█	█	█									
<b>unit 6</b>																	█								
Fieldwork																		█	█	█					
<b>evaluation</b>																									█

**Training only: 2 weeks / 11 days**

Days	1	2	3	4	5	6	7	8	9	10	11
<b>unit 1</b>	█										
Fieldwork											
<b>unit 2</b>		█	█								
Fieldwork											
<b>unit 3</b>				█	█						
Fieldwork											
<b>unit 4</b>						█	█				
Fieldwork											
<b>unit 5</b>								█	█		
Fieldwork											
<b>unit 6</b>										█	█
Fieldwork											
<b>evaluation</b>											█

# 1 Context

## **1.1 Introduction**



### 1.1.1 Introduction

Promoting local economic development is important but also extremely complicated. Quite a number of projects that aim to improve economic activities don't achieve their objectives. Often this is due to insufficient knowledge and insight during the identification phase of the interventions.

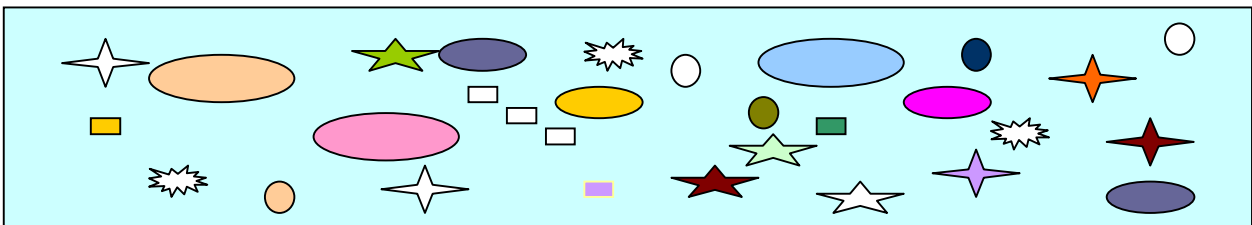
CAPSA offers a methodology and tools to look and analyse parts, or sub sectors, of an economy. It helps to understand the context and builds your knowledge about the sub sector, providing you with in-depth knowledge of the sub sector and its actors. Once you know all the ins-and-outs of the sub sector, CAPSA assists you in designing appropriate project interventions. We will therefore spend considerable time researching and analysing the situation, before we actually will identify and design project interventions. Yet, this investment will pay off with more effective and more efficient project interventions.



**Understanding takes time but pays off at a later stage**

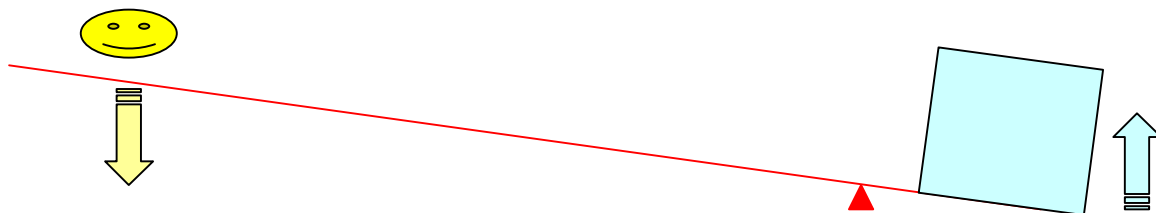
Understanding and designing cannot be done in isolation. We will have to go out and talk to the actors: the entrepreneurs, their clients, institutions and many others. CAPSA offers tools and structures for this process that requires your active participation: you as an individual, from you as a group doing this study together, as well as from your organisations that are supporting you in this process. We will be spending more time in the field than inside this room: CAPSA is a practical learning methodology and it can only be learned practising.

Even though we will have defined a certain target or client group, we will have to look at all the actors active in that sub sector: from micro enterprises to multinationals, from suppliers to consumers and from producers to traders. Only if we understand the roles, performances and intentions of all actors, we can do something for our target group. Although CAPSA can be applied for any any target group, it is written as if “small producers” are the main target group.



**Understanding all actors, not only our target/client group**

Once we understand how it functions, where the constraints are and what opportunities exist, can we identify, design and implement interventions that address them! These interventions should not only be sustainable, effective and efficient, but should be “the smallest intervention possible with maximum impact on a maximum number of enterprises: the leverage effect!”



**Uplifting: maximum output with minimal input!**

### 1.1.2 The building blocks – unit 1 to 6

We will start with the concept of entrepreneurship; what is it and how can we recognise true entrepreneurship? After all, they are the ones that will have to make things happen; they are our target group and we must be able to understand their way of reasoning and functioning. We will also spend some time on identifying and determining classifications and definitions of sectors and enterprises. We will need workable definitions and we must ensure that we are talking the same language, what is a small producer?

Unit 2 prepares the foundation: it explains about the basics of businesses, starting with the types of markets and segments, followed by the four strategic elements that each business may use. We must understand them because they often provide a lead as to constraints and missed opportunities. In the same chapter one unit is dedicated to the practice of interviewing: interviews will be our main source of information and we must make sure we get the most out of this time-consuming tool. With this new knowledge we will go out and interview our small enterprises.

Unit 3 is the corner stone of the course: we will learn how to make “a map” of the sub sector: such a map will tell us how the sub sector functions, who does what, where are constraints and where are the blanks? We will translate the information we obtained during our interviews on the map so that we obtain an overview of the various product and money flows in the sub sector. For this we also require an efficient database and therefore one part of this chapter is dedicated to the design of the database. Last but not least, we will hold interviews with suppliers, consumers and key informants to complement and complete our knowledge of the sub sector.

Unit 4 provides the practical tools for analysing the sub sector and its map: how to calculate profit margins and how that can contribute to a proper sector analysis. The SWOT analysis is then presented and applied to this subsector; providing us with directions for designing interventions. Before that, we verify whether all criteria have been met in the last module of this unit. Last but not least, we will organise a workshop with the entrepreneurs to present and discuss our findings.

Unit 5 assists us with comparing the needs of the sub sector with the various active organisations; who does what and where are the gaps? Thereafter we shall go through a number of cases that will enlarge our horizon and train us in the various possibilities.

Unit 6 deals with the final analysis of the sub sector and the actual identification and design of our intervention. Through scenario development and using all the information obtained, we will identify the most appropriate intervention for the sub sector. Last but not least, we will structure the intervention into a structured project proposal.

## **1.2 Entrepreneurship**

## 1.2 Entrepreneurship

### 1.2.1 Introduction

Let us have a look at two producers, Mr Johnson and Mr Peterson:

**Mr. Johnson**, 46 years of age, had been working for AgriCom as a carpenter for more than 16 years when he got laid off 8 years ago.

At that age and with the economy in decline, he had no chance of finding another job. He had only gone to school for three years and had started working as a labourer on the farms there after. Later he had been trained on the job as a carpenter.

Of course there was never much to do at work and he had started doing private jobs for clients in the neighbourhood. He could do this very cheap because he used the tools and materials from the company. Thus, when he was without a job, he continued the same way at home, having taking the tools from work home. He has been able to survive and is not doing all that bad.

Mr. Johnson even has an assistant who he pays when ever he sells something. A bit of a problem is that his tools are worn out and he can't afford to buy new ones. One tool costs more than he earns in a month.

It would have been so easy at AgriCom!

**Mr. Peterson**, 34 years of age, is a tinsmith and has his own workshop for some years. He did 4 years at school and in his spare time learned the trade from his uncle who was the village blacksmith.

Later he went to town and did all kind of odd jobs, finally ending up at MetalCom as a metal worker. He started doing small jobs outside working hours and sold his products easily. He then borrowed money from his father, bought a finishing-machine and started his own workshop producing buckets.

His business grew and he employed several tinsmiths. When the price of galvanised sheets became more expensive and people couldn't afford the buckets, he started buying roofing sheets and hammered them flat. The cheap buckets produced from those sheets he sold easily.

Now that competition in town becomes stiffer, he is looking for a credit which he wants to use to start travelling to the districts to exchange his buckets for farm products, which he then will sell in town.

But, credits are expensive and not easy to get !

- What are the differences between Mr Johnson and Peterson?

All entrepreneurs are self employed  
but  
not all self employed are entrepreneurs

**1.2.2 Am I an entrepreneur?**

Place a mark on each of the following lines at the point where you see yourself!

..... 

				X	
--	--	--	--	---	--

 .....

I have confidence in myself 

--	--	--	--	--	--

 I have no confidence in myself

I am a leader 

--	--	--	--	--	--

 I am a follower

I am creative 

--	--	--	--	--	--

 I am not creative

I like to take risks 

--	--	--	--	--	--

 I try to avoid risks

I do not like to gamble 

--	--	--	--	--	--

 I like to gamble

I think about the future 

--	--	--	--	--	--

 I think often about the past

I decide very quickly 

--	--	--	--	--	--

 I think three times before deciding

I try to do more than I planned 

--	--	--	--	--	--

 I just do what I planned to do

I like to make profit 

--	--	--	--	--	--

 I do not attach value to profit

I know what my business goal is for the coming year 

--	--	--	--	--	--

 I will just see how my business will develop

I like to do work with others 

--	--	--	--	--	--

 I like to work alone

I try to do what others tell me 

--	--	--	--	--	--

 I go my own way

### 1.2.3 Are you an entrepreneur?

Place a mark on each of the following lines at the point where you see yourself!

- |       |  |  |
|-------|--|--|
| 1     | I like to work in a team   | I like to work by myself   |
|       | 5    4    3    2    1    0   | 1    2    3    4    5  |
| <hr/> |  |  |
| 2     | I like to work intensely for sustained periods on things that interest me  | I like to work at a steady pace  |
|       | 5    4    3    2    1    0   | 1    2    3    4    5  |
| <hr/> |  |  |
| 3     | I believe external factors are the prime ones in deciding what will happen | I believe I can make things happen if I really want to                         |
|       | 5    4    3    2    1    0   | 1    2    3    4    5  |
| <hr/> |  |  |
| 4     | I like to feel that I'm building something for the future                  | I like to get results quickly  |
|       | 5    4    3    2    1    0   | 1    2    3    4    5  |
| <hr/> |  |  |
| 5     | I like to set targets for myself every month, week and day                 | I like to take work as it comes  |
|       | 5    4    3    2    1    0   | 1    2    3    4    5  |
| <hr/> |  |  |
| 6     | It's not important to measure how I'm doing                                | I like to measure how I'm doing by how much money I make                       |
|       | 5    4    3    2    1    0   | 1    2    3    4    5  |
| <hr/> |  |  |
| 7     | I like to stay with a problem until I work it through                      | I prefer to move on to something else rather than get bogged down in a problem |
|       | 5    4    3    2    1    0   | 1    2    3    4    5  |
| <hr/> |  |  |
| 8     | I don't accept failure   | I accept that failures are an unavoidable part of life-like to learn from them |
|       | 5    4    3    2    1    0   | 1    2    3    4    5  |
| <hr/> |  |  |

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9	I like to know all the time how I'm doing	I prefer action to analysing past performance
	5 4 3 2 1 0	1 2 3 4 5
10	I prefer that other take prime responsibility for the success or failure of events	I like personal responsibility for the success or failure of events
	5 4 3 2 1 0	1 2 3 4 5
11	I prefer not to discuss my affairs with outsiders	I like to ask advice from experts, listen carefully and act as appropriate
	5 4 3 2 1 0	1 2 3 4 5
12	I'm always setting standards for myself, and raising them as I achieve my aim	I prefer others to set standards, to let things work out as well
	5 4 3 2 1 0	1 2 3 4 5
13	I need to be really certain about the future	I can cope with uncertainty about important things
	5 4 3 2 1 0	1 2 3 4 5
14	I like to be totally committed to what I do	I prefer to live without too many commitments
	5 4 3 2 1 0	1 2 3 4 5
15	I like people to think that I will do what I say I will do	It's not always possible to keep my promises, unforeseen event can change priorities
	5 4 3 2 1 0	1 2 3 4 5
16	I like to play it safe	I like to take calculated risks
	5 4 3 2 1 0	1 2 3 4 5
17	I like to measure the pros and cons of a risk before taking it	I like to take a gamble
	5 4 3 2 1 0	1 2 3 4 5

### 1.2.4 Characteristics of real entrepreneurs

Which of the characteristics do you consider most important?

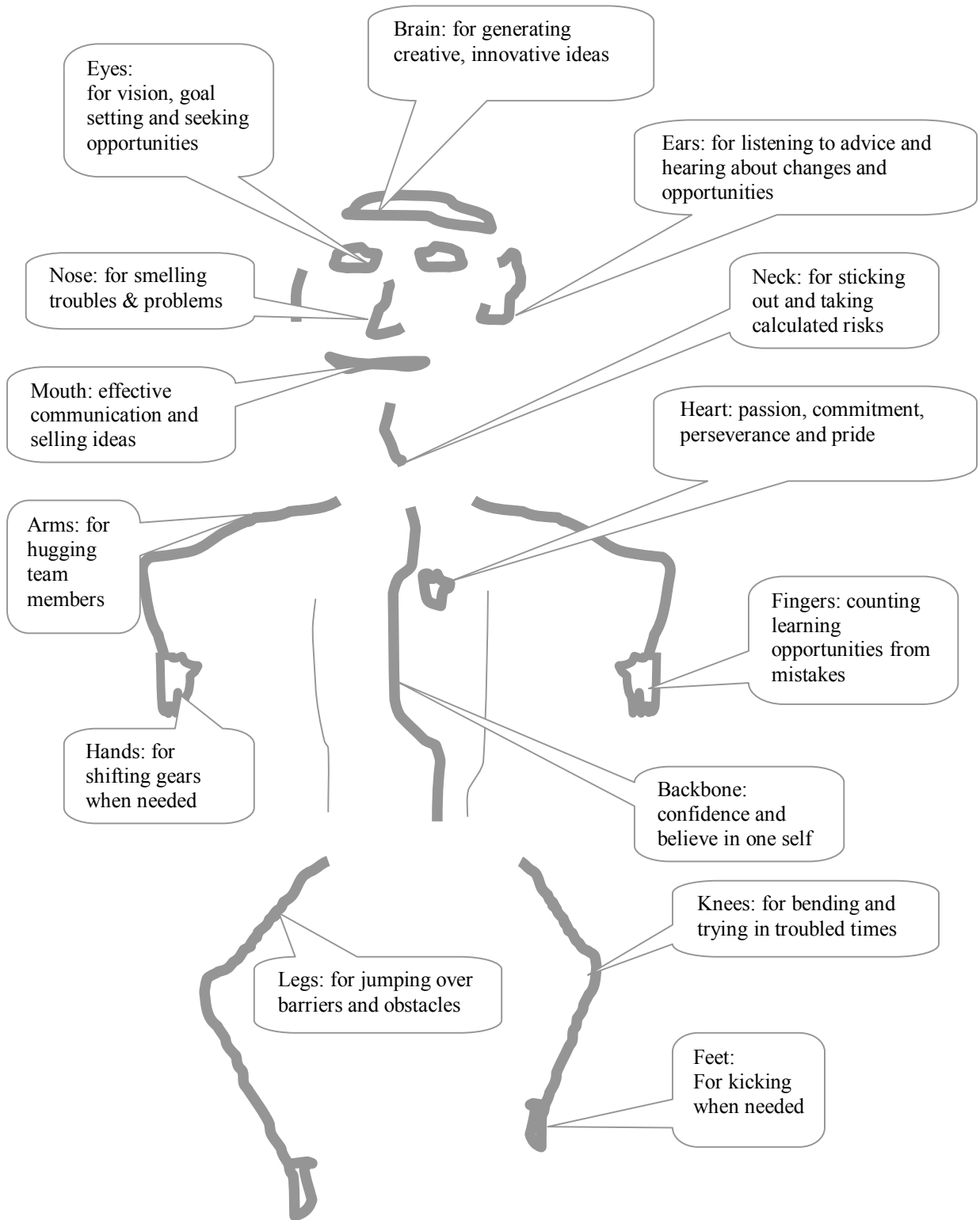
<b>Initiative</b>	<ul style="list-style-type: none"> <li>• Takes actions that go beyond job requirements or the demands of the situation.</li> <li>• Does things before being asked or forced to by events.</li> <li>• Acts to extend the business into new areas, products or services.</li> </ul>
<b>Sees and acts on opportunities</b>	<ul style="list-style-type: none"> <li>• Looks for and takes action on opportunities.</li> <li>• Sees and acts on opportunities (business, educational or personal growth).</li> <li>• Seizes unusual opportunities to obtain financing, equipment, land, workspace or assistance.</li> </ul>
<b>Persistence</b>	<ul style="list-style-type: none"> <li>• Takes repeated action to overcome obstacles that get in the way of reaching goals.</li> <li>• Takes repeated or different actions to overcome an obstacle.</li> <li>• Takes action in the face of a significant obstacle.</li> </ul>
<b>Information seeking</b>	<ul style="list-style-type: none"> <li>• Takes action on own to get information to help reach objectives or clarify problems.</li> <li>• Does personal research on how to provide a product or service.</li> <li>• Consults experts for business or technical advise.</li> <li>• Seeks information or asks questions to clarify what is wanted or needed.</li> <li>• Personally undertakes research, analysis or investigation.</li> <li>• Uses contacts or information networks to obtain useful information.</li> </ul>
<b>Concern for high quality of work</b>	<ul style="list-style-type: none"> <li>• Act to do things that meet or beat existing standards of excellence.</li> <li>• States a desire to produce work of high quality.</li> <li>• Compares own work or own company's work favourably to that of others.</li> </ul>
<b>Commitment to work contract</b>	<ul style="list-style-type: none"> <li>• Places the highest priority on getting a job completed.</li> <li>• Makes a personal sacrifice or expends extraordinary effort to complete a job.</li> <li>• Accepts full responsibility for problems in completing a job for others.</li> <li>• Pitches in with workers or works in their place to get the job done.</li> <li>• Expresses a concern for satisfying the costumer.</li> </ul>
<b>Efficiency orientation</b>	<ul style="list-style-type: none"> <li>• Finds ways to do things faster or with fewer resources or at a lower cost.</li> <li>• Looks for or finds ways to do things faster or at less costs.</li> <li>• Uses information or business tools to improve efficiency.</li> <li>• Expresses concern about costs vs. benefits of some improvement, change or course of action.</li> </ul>



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<p><b>Systematic planning</b></p>	<ul style="list-style-type: none"> <li>• Develops and uses logical, step-by-step plans to reach goals.</li> <li>• Plans by breaking a large task down into sub-tasks.</li> <li>• Develops plans that anticipate obstacles.</li> <li>• Evaluate alternatives.</li> <li>• Takes a logical and systematic approach to activities.</li> </ul>
<p><b>Problem solving</b></p>	<ul style="list-style-type: none"> <li>• Identifies new and potentially unique ideas to reach goals.</li> <li>• Switches to an alternative strategy to reach a goal.</li> <li>• Generates new ideas or innovative solutions.</li> </ul>
<p><b>Self confidence</b></p>	<ul style="list-style-type: none"> <li>• Has a strong belief in self and own abilities.</li> <li>• Expresses confidence in own ability to complete a task or meet a challenge.</li> <li>• Sticks with own judgement in the face of opposition or early lack of success.</li> <li>• Does something that is felt to be risky.</li> </ul>
<p><b>Assertiveness</b></p>	<ul style="list-style-type: none"> <li>• Confronts problems with other directly.</li> <li>• Tells others what they have to do.</li> <li>• Reprimands or disciplines those failing to perform as expected.</li> </ul>
<p><b>Persuasion</b></p>	<ul style="list-style-type: none"> <li>• Successfully persuades others.</li> <li>• Convinces someone to buy a product or service.</li> <li>• Convinces someone to provide financing.</li> <li>• Convinces someone to do something else that (s)he/ would like that person to do.</li> <li>• Asserts own competence, reliability or other personal or company qualities.</li> <li>• Asserts strong confidence in own company's or organisation's product or services.</li> </ul>
<p><b>Use of influence strategies</b></p>	<ul style="list-style-type: none"> <li>• Uses a variety of strategies to affect others.</li> <li>• Acts to develop business contacts.</li> <li>• Uses influential people as agents to accomplish own objectives.</li> <li>• Selectively limits the information given to others.</li> <li>• Uses a strategy to influence or persuade others.</li> </ul>

### 1.2.5 Portrait of an entrepreneur



## **1.2.6 What makes somebody a successful entrepreneur?**

### **Creativity and innovativeness**

Entrepreneurs believe that there are always new and better ways of doing things. They are creative. Often their ideas may be wild or fancy but this merely indicates their preoccupation with the new and the innovative. They are never discontented with the present, no matter how comfortable that is. They are imaginative about the products that they sell. They dare to be different in the way they make and sell products.

### **Knowledge and experience**

Although many successful entrepreneurs did not reach high school, much less college, all of them are knowledgeable. They learn about it well enough so that they do not depend on "experts". They also recognize the value of current events: what is going on, where and why. This is why they go ahead much earlier than most people. They get informed. The knowledge they get from others makes them wiser.

On top of this knowledge many starters have gained a wealth of experience while they were employed in a business. Even a job as a civil servant will give an individual valuable work experience and insights on what is going on in the business world and what may be required from a person to become successful.

### **Managerial abilities**

The entrepreneur is a leader. He manages his people in a way that makes them willing and able to do things for him. While he definitely controls the business, he is able to delegate some functions so that he has more time for creative activities, such as improving his product, looking for new markets or expanding his enterprise. He is rational rather than emotional about managing his business. In the face of pressure he decides and acts on the basis of what will work best for the business.

For instance, when hiring, he hires on the basis of expertise and resource potential for the business, rather than on the basis of friendship or relationship. Unless it will do the business much good, he is not ready to compromise on standards and policies simply because he does not want to hurt subordinates. He is decisive and firm, strict but fair, all to attain what he wants to get.

### **Persistence and hard working**

The entrepreneur pursues his goals to the best of his ability. He runs after it as if his very existence depends on it, harnessing for it all his talents, skills, abilities and emotions. His involvement is total. He persists, perseveres and works so hard even in the face of much adversity. He cannot stand unfinished tasks. No stress is too great for him for he thrives under stress.

### **Energy and mobility**

Entrepreneurs make the world go round. Their energy is catching. They work beyond eight hours daily, much more than the normal capacity of most people. They work and drive themselves so hard it is a wonder they are still alive. They also tend to be mobile. Boring, routine jobs do not attract them. They are never content with the ordinary.

### **Goal setting and desire to be successful**

Once he has set his mind on a goal, the entrepreneur imagines how he would feel if he should succeed or fail. He expresses these desires to himself and to others around him. His emotional involvement with the goal is total. The goal means so much to him that he thinks about it mostly in terms of winning. He gets so preoccupied with winning that he plans his strategies and tactics well in advance. Fearing failure, he identifies possible obstacles and barriers to the goal and prepares himself to prevent or overcome them. However, he remains optimistic. He is so hopeful and determined in succeeding that he sees the future as bright and promising, never dark and gloomy.

### **Attitude towards risk**

The entrepreneur likes to win and to win the hard way. That means he never sets out on anything that is either too risky or too easy. He likes challenging ventures, those that involve moderate chances for success or failure. He feels happier and more pleased with himself when he succeeds in a task where others fail or fear to enter. Unlike the ordinary man, he does not shun risks but almost seeks them. He assesses the risks. He asks himself: "Do I have enough knowledge, expertise, money and personnel to carry out such a plan? If not, what can I do to make up for the inadequacy? Is the missing element essential to make the business succeed or is it possible to go on without it?"

### **The use of feedback**

Entrepreneurs consistently want to know how well they are doing, so that they are often called recognition seekers. They delight in knowing that they have done a splendid job. However, they do not seek feedback just for the pleasure, but rather to know more about how they perform. Whether positive or negative, the feedback is a welcome input to help them produce better and accomplish more. They always view events as learning opportunities. They look for nasty feedback, digest it and act so they cease to be pitfalls in the future. Because they are open to feedback they are flexible. They do not stick rigidly to plans when they have ceased to be workable. Even in planning the business they consult with others to gain feedback about goals.

### **Personal responsibility for actions: decision making**

The entrepreneur wants to be the one responsible for a job well done. He cannot sit in a team as a hardworking member while another gets all the glory that winning brings. He leads and makes things happen. He originates ideas and action. He takes the initiative. While others go on dreaming of great things, he gets things done. He believes that he is personally responsible for the way his life turns out to be. Success to him is a product of personal effort, not luck or fate.

### **Self reliance & self confidence**

Entrepreneurs are strong, they are tough. They have faith in their ability to win and they show it. While the rest of the world regards the environment as overpowering, the entrepreneur views it as something that can be conquered. He is willing to plunge into the unknown. They seem to overestimate their capacities. Overconfident? In a very real sense, they are. It is no surprise to discover that a *successful* entrepreneur has a history of failure. Many times they overestimated themselves. But they did not give up when they failed. He can get things done because he is self-reliant and independent. Money, friends, contacts -all of these merely augment and support what the himself has to offer: hard work, ambition and competence.

**Ability to persuade and motivate**

An entrepreneur can talk in a way that excites other people. He might be poor, with no land, no car, no big family name, no master's degree. But he dreams, and he talks of his dreams in a way that makes other people dream with him. Therefore, a relative lends him a land title, a friend lends him some money, another friend lends him a car. He presents his idea and achievements to the bank manager and walks away with a loan. He talks to competent skilled hands around the neighbourhood, promises them a good future with him, and off they go to start a business on a small pay and a big shared dream. He can influence and inspire people.

**Achievement orientation**

Entrepreneurs are interested not only in the end result but in the process of attaining it as well. They are concerned with excellent performance, setting high standard for themselves. Once they have committed themselves, they pursue it with a flourish, so to speak. In business, therefore, they actually do not work for the profit (they use it as a feedback mechanism to tell them how well they are doing) but for the growth potential of the firm.

## **1.3 Classifications**

### 1.3 Classifications

#### 1.3.1 Introduction

*The car manufacturer buys steel sheets and creates a car.*

*The supermarket buys products from suppliers and sells them to the public.*

*The shoemaker repairs shoes.*

The difference between the three is huge: the size of their operations is different, the complexity of their operations is different, but most important: their functions differ!

The three have a lot in common: they have commercial activities, they are all entrepreneurs, they all 'do something' what their clients need!

#### 1.3.2 Three sectors

However, that 'doing something' differs and that we use to distinguish between the three sectors:

##### 1 Manufacturing

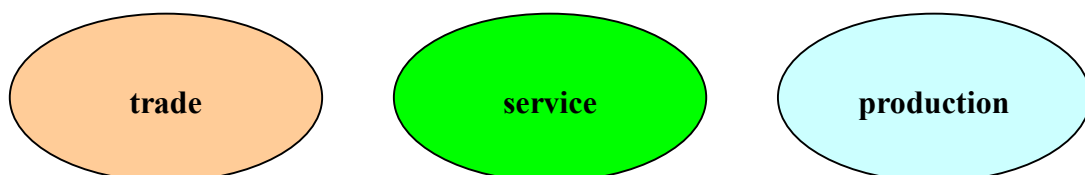
The main function of the car manufacturer is to produce cars: he manufactures cars (the product) by *physically transforming* the steel sheets (the raw material). Of course he sells the cars, but his main function is to produce: he is therefore active within the sector of manufacturing.

##### 2 Trade

The main function of the supermarket is to sell products; it does not transform products physically but only buys and sells them: it might buy in large quantities and sell in small quantities; it makes profit by *trading products*: it is therefore active within the sector of trade.

##### 3 Service

The shoemaker does not transform basic materials into new products nor does he buy and sell, he repairs shoes: he *improves* the quality of the product. The shoemaker is therefore active within the sector of services.



- In which sectors would you classify these entrepreneurs?

	manufacturing	trading	servicing
farmer			
transport company			
consultant			
carpentry workshop			
street vender			
butcher			

### 1.3.3 Numerous sub sectors

*The car manufacturer buys steel sheets and creates a car.*

*The supermarket buys products from suppliers and sells them to the public.*

*The shoemaker repairs shoes.*

We can also distinguish between the three in terms of their basic raw materials:

- the car manufacturer is active in the *steel* industry
- the supermarket is active in the *food* industry
- the shoemaker is active in the *leather* industry

In this case we talk about sub sectors: all players that are active with the same raw materials.

- In which sub sectors would you classify these entrepreneurs?

	sub sector
farmer	
transport company	
consultant	
carpentry workshop	
street vender	
butcher	

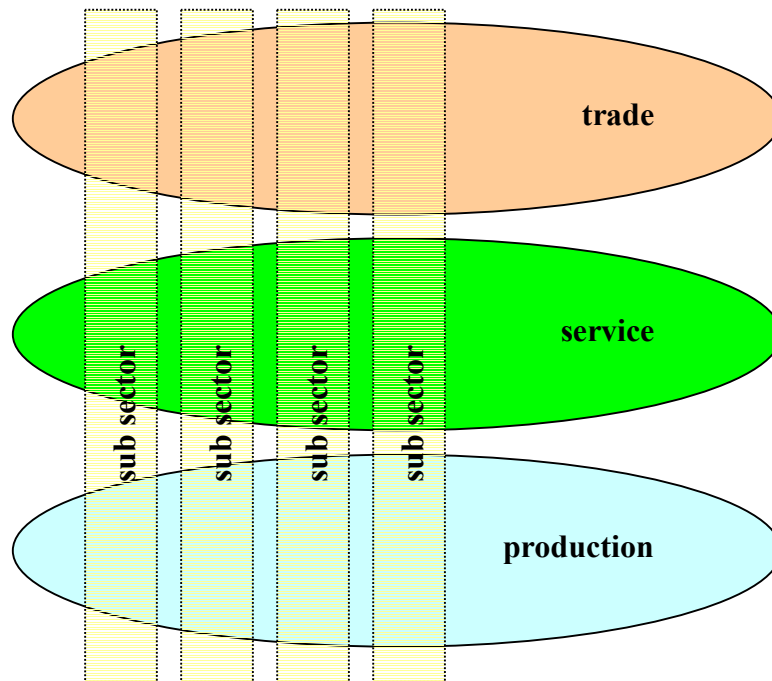


An entrepreneur can thus be classified

within a sector (manufacturing, trading or servicing)  
**and**  
 within one of the numerous sub sector (timber, goats, steel, etc.).

*People can be classified as male or female **and** as young or old*

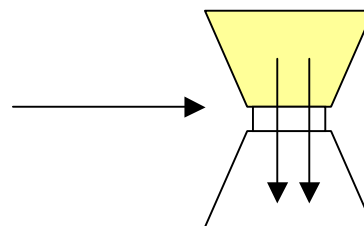
We could visualise the two classifications as follows:



- Name at least 10 sub sectors in your province

In this study we will analyse sub sectors and that implies that we not only look at the producers, but we also look at the other actors within the sub sector: the traders and the service providers. The functioning of these other actors may very well influence the functioning of the producers. In principle all products need to be sold and if the bottleneck lies in the trading of the products of the producer, we might resolve the trading problem and thereby thus resolve the constraints of the producers.

*trading bottleneck becomes producers problem*



### 1.3.4 The size

The size of the enterprise is also an important factor when we undertake a sub sector analysis.

*Children have other needs than adults  
and these adults have other needs than the elderly*

*Children are very small when they are born; they breath by themselves but need feeding. Infants learn to walk but have some difficulties in coordinating all functions. They grow up and become mature: they start relationships, they get used to tools that will ease their life. The elderly do not do that much themselves, but they are respected for their wisdom, they advice their sons and steer the family!*

Companies also are born and some grow into huge enterprises.

Bill Gates started his Microsoft in his garage and now manages tens of thousand employees. The growth stage companies are in, determines the way they function and thus the needs they feel. You can imagine that Bill Gates from his garage had to design, produce, buy and sell everything himself; now his company houses designer departments, production companies, logistical departments and huge marketing departments. His needs are different. Initially he was probably trying to survive, doing as much as he could himself. Now he might be delegating most operational issues and focus on long term strategies, for which he hires the most expensive consultants.

Not all companies will grow into huge enterprises. Some entrepreneurs prefer to not to grow but remain with a small yet flexible company. Following the growth path is not a must!

That growth stage is often expressed in the size of the company: micro companies function differently from huge companies and thus have other needs.

We talk about four categories:

- micro
- small
- medium
- large enterprises.

The main criteria that determine those classifications are:

- the number of employees
- the turnover of the company
- the assets of the company

These three criteria however may differ per country, per sector and per sub sector!

*A firm with twenty layers might be a large enterprise whereas a construction company with twenty labourers is probably one of the smallest companies in the sector.*

*A car manufacturers with a turnover of only 200 million dollars is probably just a beginner whereas a bicycle producer with a turnover of 200 million is a large enterprise.*

*A lease company with 200 cars is probably a large enterprise in Gambia whereas it would be one of the smallest companies in the United States.*

*A supermarket employing 10 people will be a medium player in the sub sector, whereas the farmer who employs 10 people will be a small farmer.*

We therefore don't worry that much about standards: we adjust the criteria to our sub sector by choosing the value that is most decisive! For most sub sectors in most countries we often follow the following criteria:

	<b>micro</b>	<b>small</b>	<b>medium</b>	<b>large</b>
<b>employees</b>	<5	5-25	25-75	>75
<b>turnover in US\$</b>	<10.000	10.000-50.000	50.000-250.000	>250.000
<b>assets</b>	<3500	3500-25.000	25.000-100.000	>100.000

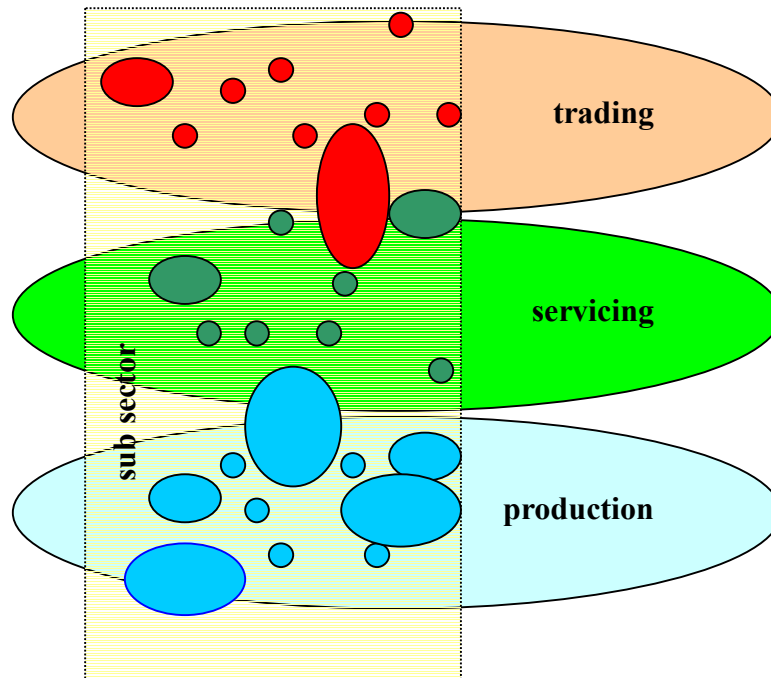
Micro enterprises are mainly concerned with the primary process (producing, trading or servicing) and their objective is short term: they want to secure their income. With larger enterprises we notice that their secondary processes become more important (supply management, people management, planning) and their objective is more longer term: they want to grow and increase their profits.

- Analyse your sub sector and define workable criteria.

The combination of these three criteria characterise the enterprise: the growth stage, the focus, the functioning and the needs. We should be careful not to copy or use criteria that are set by others: they might have defined these criteria for other reasons. The classification of the tax department was set up to "manage" the collection of taxes, not to characterise the growth stages. In some countries we can see that they use three categories (A, B and C) but their definitions differ: we even see that certain sub sectors and type of enterprises (farmers, cooperatives) are treated differently: not because they function differently, but because the government would like to tax them different from other companies for policy reasons. Such a classification does not assist us with our study and that is why we design our own classifications.

### 1.3.4 Characterisation

We combine all the criteria to describe the actors in our sub sector



There are many small and only a few bigger companies: they are either producers, service providers or traders, although a few of the bigger ones seem active with various production, trade and servicing activities. Our interest lies with the smaller producers but we cannot analyse their functioning, let alone improve it, without looking at the bigger companies and the other sectors!

# Tasks Unit 1

## Tasks Unit 1

### 1. The characteristics of true entrepreneurs have been discussed:

- What you consider to be the 5 most important entrepreneurial characteristics.
- Prepare some questions that will enable you to measure the degree of entrepreneurship.

### 2. The sector classifications have been discussed:

- Give some arguments why you should or should not focus on production, service or trade.
- Give some arguments why you should or should not focus on micro/small enterprises or medium/large enterprises.

### 3. Describe your sub sector:

- How does your sub sector function: from raw material to end consumer.
- The actors in the chain: the type, numbers and volumes.

### 4. Give arguments:

- Why your sub sector does or does not have potential.
- Why your sub sector should receive our attention.

### 5. Interview 5 entrepreneurs:

- Choose a good sample of 5 entrepreneurs.
- Prepare an interview with a small entrepreneur that includes the questions from task 1 and that will help you to answer the questions 2 to 4 and 6.

### 6. Give arguments:

- Why you consider the interviewed entrepreneurs to have or not to have an entrepreneurial attitude.
- Why we should or should not focus ourselves on entrepreneurs that have sufficient entrepreneurial characteristics.
- Why we should or should not focus ourselves on entrepreneurs that do not have sufficient entrepreneurial characteristics but do have potential in this field.
- Why we should or should not focus ourselves on entrepreneurs that do not have sufficient entrepreneurial characteristics and do not seem to have any potential in this field.

## **2 Business**

## **2.1 Business Principles**



## 2.1 Business Principles

### 2.1.1 Introduction

Let us have a look at a small furniture production company in a little town. Mr. Timbo, the owner, is a professional craftsman and produces beautiful furniture. His workshop is reasonably equipped, albeit not with the most modern machinery. Yet, the production is very labour intensive and he never really bothered to buy the latest state of the art machines: it has been like this for almost a decade now. He employs some five workers who he pays whenever he has work for them. All in all, the workshop has been providing a stable income, but in the recent past the work is getting less. Mr. Timbo has been discussing this with his sons, Paul and Moses, both working as carpenters with their father. Let's look at their argumentation:

#### Paul

We have to invest in new machines, bigger ones, so that we can produce more furniture at a lower cost. That will cost a lot of money but then we can produce double the volume we now produce, and more important, we can do so in half the time. So we can produce four times as much!

We the two sons take care of the construction parts, our father does the carvings and the labourers do the sandpapering and finishing. In that way, our manual production will become a modern production line. Of course it implies we will make standardized furniture.

I reckon we can drop the price from \$900 to \$700 per average piece!

#### Moses

Well that looks very promising, but I doubt whether the price will drop that much. For these machines you have to invest a lot of money, for which we have to get a loan and repay a lot of money every month to the bank. Borrowing is expensive you know.

It would be much better if we no longer make use of our workers, but do everything ourselves. That way we save a lot of money, and the boys don't do that much anyway.

So, each one of us will concentrate on a special type of furniture and become a specialist therein so that production time is shorter. By no longer making the carvings we will save time also.

In that way, I believe we will save some 30% and so we can drop the price also to some \$700 per piece!

The discussion between the two sons continues along these lines and the father concludes after half a day:

*Well, I have listened to your argumentation now and I must say that both of you make sense. Yet, it is too early for me to take a decision. Remember your niece Maria? She now works with a bunch of NGOs doing something with economics, I suggest we ask her for advice.*

Maria, a clever woman who doesn't want to get trapped in this family dispute, refers Mr. Timbo to you!

- What is your analysis of the case, and what do you advise Mr. Timbo?

## 2.1.2 Markets

We have seen in the previous case how important it is that the producer produces products that the (potential) customer needs! Without somebody who is willing to pay for such a product it makes no sense to produce, no matter how cheap or how beautiful the product might be!!

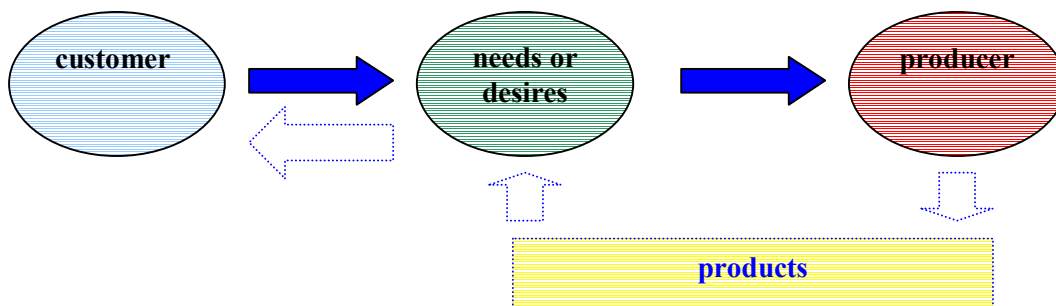
*Paul and Moses reasoned as follows:*

**The producer produces products and looks for customers to buy them:**



*But the above case learned us that it should be the other way around:*

**The customer needs products that the producer can supply:**



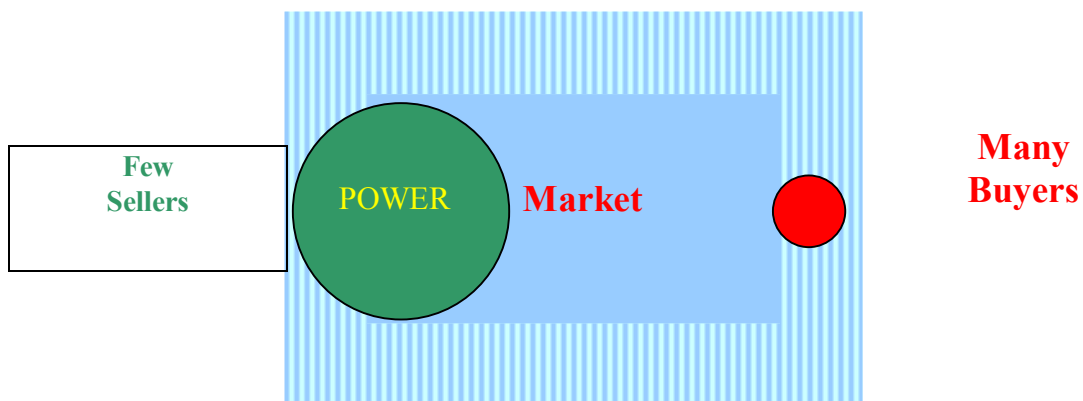
So the starting point is the customer; what does he need and how can the producer meet these needs? Can our products satisfy the customer's needs?

In only very rare cases do we deal with one customer and can we meet his specific needs. In general, we (hope to) deal with many customers. We therefore talk about markets; a *market* is a "place" where customers are looking for products that meet their demands and where producers sell their products that meet these demands. We see such markets in reality, physically, but from now on in our terminology we refer to markets in a conceptual way; *the place where buyers and sellers meet*.

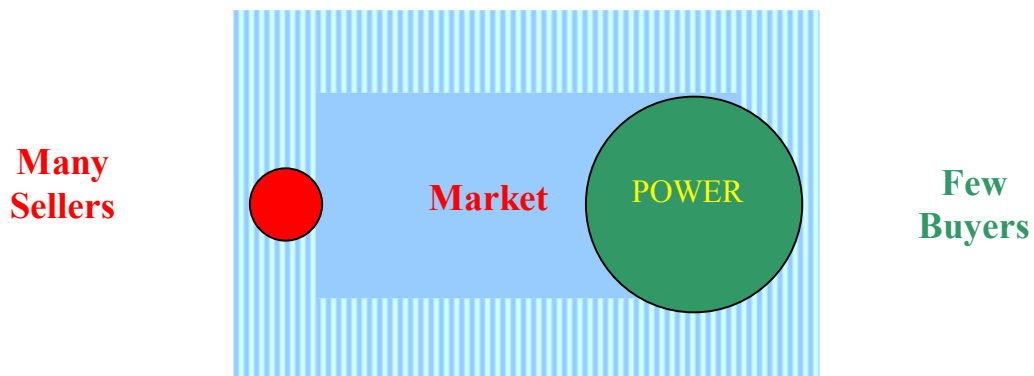
It is important we first have a closer look at these markets; in principle there are two groups that are active on such markets; the buyers and the suppliers. If there is a balance between the buyers and the sellers, both have equal powers.



But if there are only a few sellers and many buyers, than the sellers have more power and they can dominate the market: for the producers it is easy to sell their products because there are more people who want to buy them than that there are producers that sell them. So the producer determines the price and in many cases, even though the quality of the product is poor, the buyers will buy the product and so we talk about **a sellers market**:



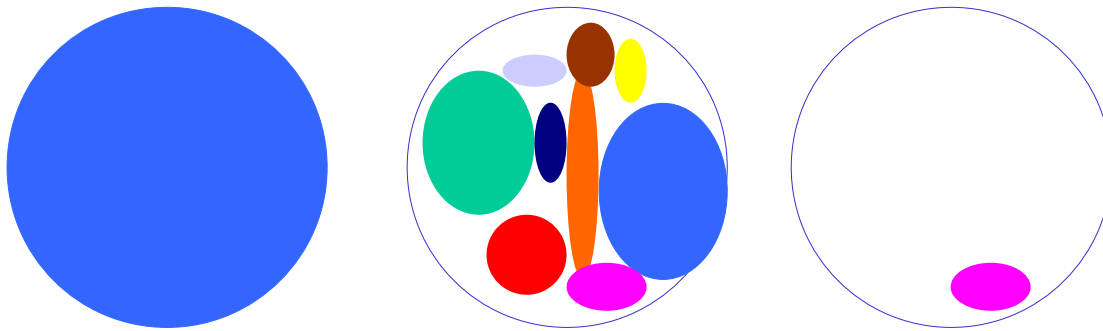
But if there are many sellers, and only a few buyers, than the buyers have the power: they can choose between the sellers, they are in a better position to negotiate prices, they can demand a better quality, and in such cases we talk about **a buyers market**.



### 2.1.3 Segmentation

In the previous section we discussed the markets and the powers of the producers and customers. When looking at the market, we actually see that not all the customers have the same needs! Some might look for high quality products for which the price is not that important, while others might look for products at a more affordable price level. It is thus important that the producer tries to distinguish between the needs of the various customers since their needs differ: can we deliver a certain product that meets the requirement of a certain group of customers?

Segmentation is a tool that might help us therein. A market segment is a group of customers that have similar characteristics: they would buy your product for the same reasons! Sub dividing the market in various segments or groups is called segmentation.



The blue circle represents all customers that are interested in the product (e.g. people need chairs).

But some (the various coloured circles in the middle) buy the chairs for different reasons! E.g. the customers in the green circle think that quality is very important, while the people in the brown circle might consider that low prices are most important. It will be difficult to make a chair that meets all requirements: a very high quality at a very low price. So it most likely that we have to compromise between price (low) and quality (high) but then do not meet the needs of both groups: neither very cheap nor of a very high quality.

If we now look at one segment; e.g. the people in the pink circle on the right, we can optimise our product to meet their specific demand. Especially in a buyers market where competition is stiff, which then often focuses on price competition, we might create our own niche; our own little market where there are customers who will buy our product. So in this case, we either make (rather expensive) high quality chairs or we make an ordinary but very affordable chair.

**Segmentation of markets = knowing your customers!**

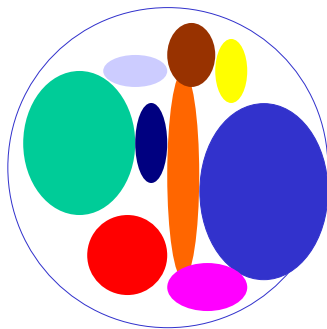
There are a few criteria that may assist you with characterising the customers and subdividing them in segments:

**Segmentation Criteria:**

Demographic	Are they single or heads of families, are they young or are they of age, are they male or are they female?
Socio economic	Do they have a high income or a low income, are they traditionally rich or have they recently made a lot of money?
Geographic	Are they living in towns or in rural areas? Are they far away from the producer or nearby?
Life style	Are they modern people or are they rather traditional, do they enjoy life or are they careful spenders?
User frequency	Do they buy the product on a regular basis or only very rare?

It is important that you realise that one criteria is not sufficient, but that it is often the mix of criteria that helps you to define your customers.

*E.g. the young high income families in town that buy sausages every Sunday are quite different from the rather poor elderly couple in the village who buy sausages when they have something to celebrate once in a while!*



Because each customer values your product differently !

When you have determined the various segments, it is time to decide whether these segments are interesting for you as a producer! In other words, can you make a profit there? That depends partly on the **competition**: if there are many competitors, it will be difficult to compete: many customers know their suppliers and why should they change and come to you?

*Have a look at the marketers; there are many selling the same products, often identical, even in price. So why should you go into buying and selling onions if there are (too) many who are buying and selling onions? In case you produce onions, could you think of another segment where there is less competition but where you might make enough profit?*

The **size of the segment** is very important too; if there are only a few customers in that segment, is it worthwhile to invest in that segment: will the customers buy enough from the producer to bring him sufficient turnover?

*Well, as a onion producer you might look at the restaurants who need onions everyday and they might be willing to buy from you (you become a regular supplier which is an advantage) but are there sufficient buyers in town? Since you will concentrate on these clients you do need enough production to satisfy all your customers (to remain reliable!) but you should also be able to sell all your production and not only a small portion!*

But most important, you must be able to reach the segment, the customers; you must have **access** to them!

*As a onion producer you might also think of larger institutional buyers such as hospitals and the army. However, if they have centralised buying offices in the capital and only deal with large commercial farmers who produce the full range of vegetables and have transport to deliver it to their doorsteps in four provinces, you might have identified a profitable segment but you will have no access to it!*

#### **2.1.4. Four strategic elements**

Once we know what the customer in the various segments need, we have to design strategies how we can deliver what the customer wants. These four elements are:

- the product
- the distribution
- the promotion and
- the price.

## 1 The Product

The **quality** of the product is one of the main characteristics of the product and thus is quality one of the main instruments. Quality is about delivering the same product every time so that the customer knows what he can expect; he can trust the producer to deliver a constant quality.

If a customer buys 10 apples every week he wants to be assured that he can eat them and what he despises most is that one week he can eat 9 of them and the other week he can only eat 5!

Quality is often linked to price: the higher the quality the more the customers are willing to pay for it. The main question is thus how the producer can improve the quality (at the lowest costs) in order to get a higher price for the product.

Quality is often linked to appearance.

a well sandpapered and shining piece of furniture often appears to be of a higher quality than a robust and rough chair: if the carpenter does not take any pride in making the product 'look nice' the customer wonders about the neatness of the construction itself.

The quality of the product should meet the requirements of the customer; the product should do what it is supposed to do; no less, no more.

A bread bum is supposed to remain eatable for a few days, there is no need to make it last a few weeks. Clothes that don't wear at all do not meet the requirements of most customers: they will buy new clothes anyway, so the 'higher quality' does not add value. Bread that goes off in three hours is no good either, and clothes that fall apart after one party also don't meet the requirements.

Quality can thus be an instrument to meet the customers requirements. It is also an instrument to distinguish one from the competition and/or allows one to ask a higher price. If people are willing and able to pay a higher price for quality products, this is often a very profitable strategy: the cost of improving the quality is often less than the price difference.

The **packing** of the product is an important part of the product too. Not only does it improve the attractiveness of the product, it also protects the product in storing and handling. One could even use it for promotion! Packing is in some cases more important than the product itself.

a customer buying eggs in a plastic bag runs the risk of arriving home with only a few eggs. Sausages in a sealed plastic are likely to stay eatable for a longer time than sausages wrapped in a newspaper. Tomatoes packed in a crate can be carried over longer distances than tomatoes in a carton box.

Take a look at the imported products and compare them to locally produced products. Price and quality are often comparable, and preference for imported products is often the result of the better packing! Note that one recognises certain producers, simply because their name is on the packing; the product gets an identity!

**The assortment** is also part of our product.

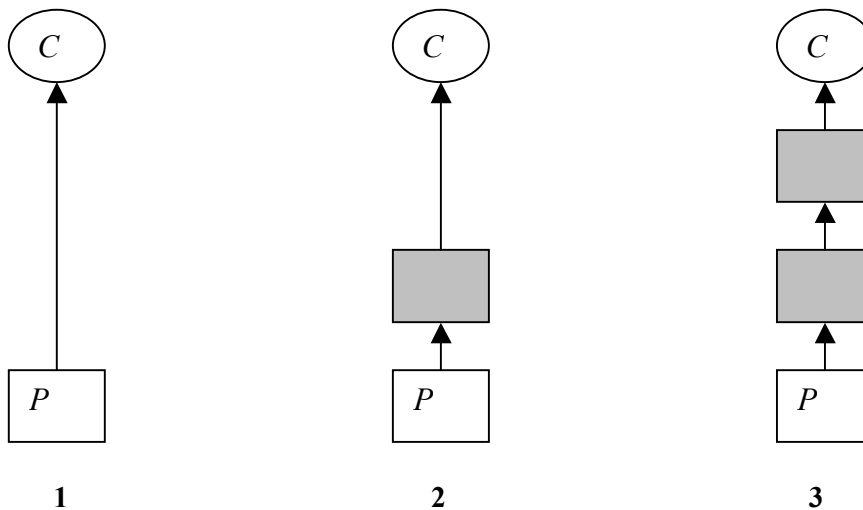
Customers prefer to have a choice from various product types. If they want to buy bicycles, they would like to choose between various bicycles: the colour, with or without a carrier, with big or small tyres, etc. Offering a larger assortment often implies higher costs (different paints, fitting parts, etc.) and these costs need to be off set to higher prices or turnover.

Customers prefer to buy various products at one time. If they have to buy vegetables, they prefer to go to one place where they can buy various types of vegetables. Few are willing to walk one hour just to buy high quality low priced tomatoes: they prefer to buy tomatoes and onions (at a higher price /lower quality) at one spot. This is even more so for the wholesalers; buying various products from various sources is much more complicated (and thus costly) than buying from one supplier.

## 2 The Distribution

Distribution is the second key element: how do the products produced by the producer reach the customer: the end user or consumer? In general one distinguishes three channels:

1. The direct channel is very short and straight forward: the producer sells directly to the consumer.
2. The second option is the short channel: the producer sells to the retailer who sells to the consumer.
3. The third alternative is the long channel: the producer sells to the wholesaler who sells to the retailer who sells to the end user.



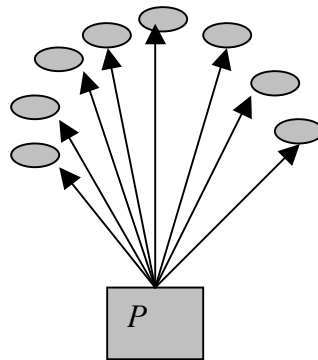
The choice of the channel depends on the efficiency, the characteristics of the sector and scale of the operations. The distributors (the wholesalers, the retailers) have three main functions:

- storing,
- transporting and
- financing.

Let us compare the three channels in relation to the three functions.

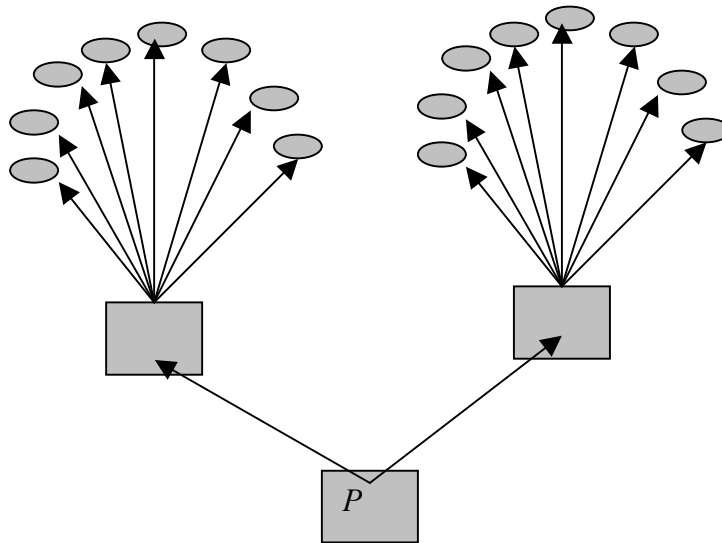


*The direct channel:* the producer has two main functions: he produces and he sells. If he sells directly to end users, it implies that the number of sales is limited: each sale will cost him time and energy and the size of each sale is limited. However, the money the customer pays for the product is entirely for the producer.



*High prices per sale but a limited number of sales*

*The indirect channels (short and long):* the main function of the producer is to produce: he sells only to a few 'intermediaries' and he gets a lower price per product: only part of what the consumer pays. However, he sells a larger volume at one sale.



*Lower prices per sale but with higher volumes per sale*

In this second channel the producer receives a lower price for each product than was the case in the first direct channel: for the difference in price the intermediary handles a few things for the producer:

- he stores the product: he will buy in large quantities from the producers and will sell in small quantities to the consumers, packing or re-packing is his responsibility.
- he transports the product, from the producer to the consumer, either in reality or in time.
- he finances the producer: he will pay the producer for the large quantity and will only sell to consumers in small quantities, a process which takes time (and costs money).

The main question is whether the producer is in a situation to perform the three functions himself with the same efficiency, time and costs, as the intermediaries. Does the higher price make up for these three functions?

### 3 Promotion

The third key element is called promotion, which covers all the activities that are related to promoting the sale of the products: advertising, public relations and promotional campaigns. The larger companies make enormous budgets available to promote their products: they all try to draw the attention of the (potential) customer to their product. For smaller companies these costly campaigns are not that interesting: it probably costs more than it brings extra sales.

The best promotion is to deliver good products that meet the requirements of the customers: if they are satisfied they will tell their family and friends, and that is promotion that doesn't cost extra money! So reputation is an important issue. Promotion is mainly about drawing attention of new customers, and that is always more expensive than maintaining one customer: that doesn't cost anything at all!

But the smaller companies can improve their sales too. Often they appear to have 'hidden' themselves in neighbourhoods. The happy customers told their friends but these friends can't find the producer! So a simple business card or a leaflet will help, as well as some signposting near or at the location.

### 4 The Price

The fourth key element is the price. The price comprises two elements: the actual amount of money that is being paid for the product and the efforts that are being made to buy it. Very often we focus on the first part, the money that is being paid, while the second part, the efforts, are just as important!

The price the customer pays for a product is the amount of money the customer pays to the producer and the time, energy and costs of getting there! Customers do compare both these price elements and that is the reason that intermediaries function: every customer knows that he spends less money if he would buy from the producer, but it would cost him too much! Companies often buy expensive imported furniture of a poor quality in stead of good furniture at reasonable prices from local producers. The reason is often "the hassle" of waiting and visiting the producer in comparison to a simple phone call to an importer!

*Before we discuss which methods exist to establish prices, we have to look at the various strategies regarding the pricing!*

The ideal situation would be where the customer is willing to pay "any price" for the product: in other words, the other elements (product, promotion and distribution) are so valuable that the actual price is not important at all! Yet, for most producers and sectors that is not the case and they are left with **two main strategies**:

1. The producer can opt to go for a pricing strategy that enables him to grow: he keeps the price as low as possible but tries to sell as much products as he can. He only makes a small profit on every sale, but by selling a lot of products, he still makes a reasonable profit.
2. The producer can opt for a pricing strategy whereby he gains the most profit per product and therefore does not have to sell that many products to make a reasonable profit.

Which strategy is most successful depends on many factors. If there are many competitors with identical products, the latter strategy will not work while the former strategy might work: with the resulting lower prices the producer will beat the competition on price. If the producer has an outstanding product (quality, service, reputation, etc) for a segment that is willing and able to pay that higher price, the latter strategy would be advantageous.

An important question for the producer is whether he would sell more if he would reduce the price per product a bit.

If a producer now sells 10 products a day with \$5 profit per product, it gives him \$50 profit per day. If he would reduce the price with \$1, in other words, reduce the profit to \$4 per product, but then would sell 15 products per day, his profit per day would be  $15 \times \$4 = \$60$  per day. He thus has improved his profit from \$50 to \$60 a day! If on the other hand, he would not make more sales due to his lower prices, he would be simply reducing his profits from \$50 to \$40 a day!

This brings us to the **price setting methodologies**.

The most basic calculation is to add up all the costs made to make the product and to add a small fixed mark-up. With that method the producer will ensure he gets a small profit on each product that he sells.

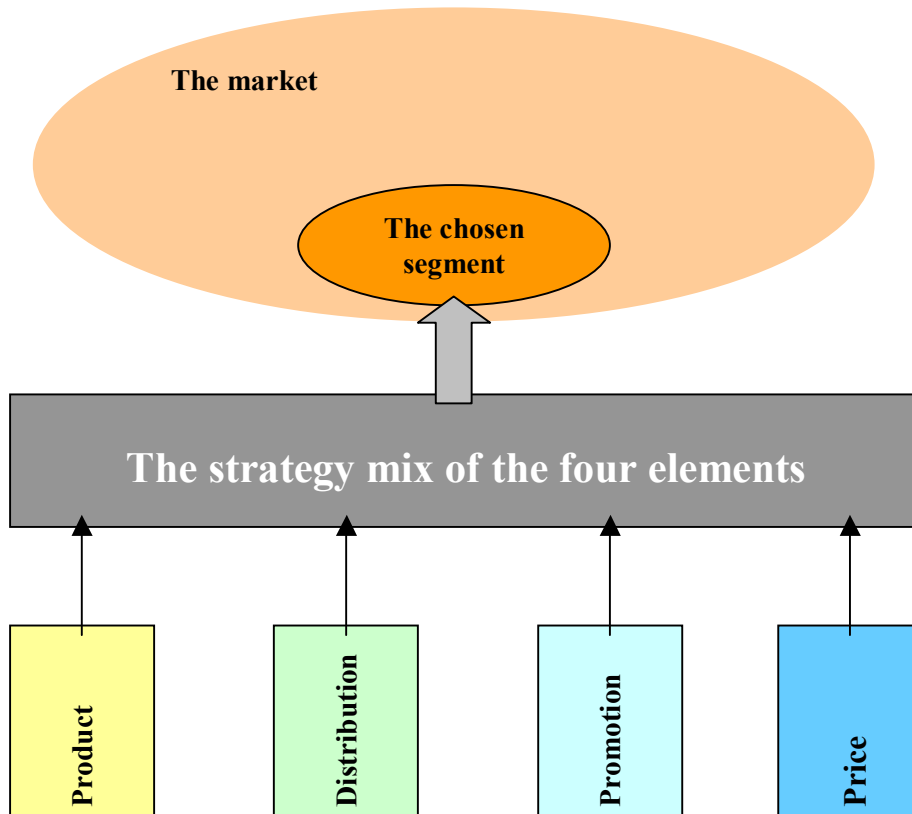
Yet, he forgets about the competition: are they selling at the same, higher or lower prices? If they sell at higher prices, he will sell a lot (he is the cheapest) but if his selling price is much lower, there would be room to increase his profits by increasing his price to just below level of the competitors. If the competitors are selling at a lower price, he will probably not sell that much, unless his other key characteristics (product, promotion and distribution) are better or different.

In that case, the producer has to look at the price the customer is willing to pay for his product! In some cases that might be less than the calculated price (costs plus mark up) and he will not sell that much: he has to find ways to reduce the costs. In other cases the customer might be willing to pay more than the established price, and thus the producer could increase his price (and profit).

The most appropriate approach is to calculate the cost price and then compare it to the competitors price (for identical products) and at the market price: the price the customer is willing to pay! Depending on the chosen market segment and company strategy each producer has to set his price.

### The mix of the four key elements

As you will have noticed, there is a relation between the various individual strategies (product, distribution, promotion and price) and the chosen market segment. It is therefore impossible to provide a blue print as to what would be the best mix. In principle any mix is possible, as long as it is suitable for the chosen segment.



**Case A      The product**

John and Peter are both carpenters, producing basic tables and chairs for the medium income group. They were both trained by the same master carpenter and in principle make identical furniture. Yet, Peter asks a higher price than John and his customers actually are willing to pay the higher price.

- Name three reasons why this might be possible?

Let us have a look at the products, the production and the differences.

For one table set John buys cheap timber for \$200. His workers don't spend too much time on the production itself (most of their time they spend on preparing the planks) and the labour cost amount thus only to some \$100. He sells the sets at \$400.

For the same table set Peter buys seasoned timber for \$250. His workers are highly skilled, do a good job within the same time, but their labour costs are \$125. He sells the sets at \$500.

- What are the gross margins of John and Peter (gross margin = income – costs)?

John reckons that if his workers would spend more time on the production, especially sandpapering and finishing the table sets, he could ask another \$50 on top of his price.

- What would be his gross margin if the workers spend 25% more time?
- Mention a few advantageous and disadvantageous for both John and Peter!

**Case B      Distribution**

Paul is a small producer of vegetables; he works all day and hardly makes an income. The average selling price of his vegetables is \$1.50 a piece. He now sells to a local shop owner. That shop owner buys from all the framers in the neighbourhood and sells it in town when he is going there anyway to buy other supplies. He pays not that much and Paul is really upset if he finds out that his vegetables are sold there for \$3.50 a piece: that's a huge mark-up for spending only a day driving while he himself is working a full year! So he wants to sell in town too!

He reckons he will have to pay some \$10 for transport one way (using a local bus) and will stay in town for a two days where he has no family but rents a room at \$10/day. He also has to eat and that costs him another \$10/day. He estimates he can carry around 30 vegetables per trip.

- What are the costs Paul faces when selling in town?
  
- What is the additional profit he makes when selling in town?
  
- What are the other advantages of selling in town?
  
- What are the disadvantageous of selling in town?
  
- What advice would you give to Paul?

**Case C      Distribution**

Emerson is also a vegetable grower and he also sells his vegetables at \$1.50 but he simply waits until somebody pops up at home. In fact, he has no worries since vegetables are in high demand and he sells easily. This way he can concentrate on the farming (*even though that is not a full time job, you can't weed all the time can you?*). Sometimes he sells a few vegetables at the local market but he doesn't like to stay there all the time. These market buyers buy at \$1,50 from him and sell it at \$2.00 at the local market. Traders from town visit this place (they travel the 10 kilometres with the bus at \$2 one way), buy on average 35 products and sell them to marketers for \$3.50, who sell it again for \$5,00 per piece.

- What are the costs Emerson faces if he would be selling to the marketers in town?
- What would be the additional profit he would be selling to the marketers in town?
- What are the other advantages of selling in town?
- What are the disadvantageous of selling in town?
- What advice would you give to Emerson?

**Case D Price**

Manuela wants to buy 50 chickens and sell their eggs. Each chicken lays on average 4 eggs a week. She now wants to determine the selling price. The food costs her \$20 per week for all the 50 chickens and she spends an additional \$5 per week on medicines. She works seven days a week (*chicken also lay eggs on Sundays!*) and she wishes to make at least \$1 a day.

- Calculate the costs price of the eggs
- What would be her selling price?

*Manuela undertakes a small competition analysis with the following results:*

In the supermarkets the price is \$2.50 per box of 10, these are directly imported from the neighbouring country or bought from one wholesaler at \$2,20 per box. At the main market the price is 20 cents, at the informal market it is 18 cents and on the street you have to pay 22 cents. These are locally produced and vary in size. Sometimes they are not available at all, but the price still stays the same.

There is one commercial farm selling directly to customers, and they sell at \$1.80 per box of ten. The quality is really good and they produce throughout the year but they rarely sell off the surplus to the public. The majority they sell to a wholesaler who then sells to the supermarkets and to other provinces.

- Make an overview of the selling prices to the public of the various types and sales outlets
- To whom or where would you advice Manuela to sell her eggs?

*Manuela undertakes a small market study and comes up with the following results:*

The main problem is that eggs are simply not available all the time.

Restaurants, hotels and the hospital have to roam the streets to get their supplies, which takes them a lot of time. There is hardly an alternative for eggs since their clients want an egg for breakfast! If they don't have eggs they offer bread and jam, not really appreciated by the customers but it costs also little; \$0,20 for one breakfast excluding preps and bread. Breakfast is included in most accommodation prices but if not, breakfast (also open to the general public) costs some \$1,50. They also offer the traditional steak (including an egg) and the price difference between ordinary steak and traditional steak is around \$1, excluding preparation.

The ordinary public buys an egg once in a while, but if it is not available they simply don't. It seems they look at it as a luxury item: whenever they have some money they buy a few eggs, the price doesn't really matter. She asked a few 'better of' buyers and she was surprised to find out that they did not really knew what the price of one egg was; they simply bought it at the supermarket when available per box or at the market at what ever price that was asked. Some more price conscious people did mention they paid around 20 cents and they would be willing to pay more (?) if the supply would be constant.

- What would you advice to Manuela?



**Case E Strategic mix**

Josh wants to start a medium sized pig farm. Josh is a friend of the family and so your advice is being asked: you have participated in a sub sector study didn't you?

What is the advice you can give to Josh? No further information is provided since (most of ) you are buying meat, so the information is known. *In case you are missing information: you state that you miss that information and you assume certain facts.* In principle everything is possible, as long as you can reason your argumentation!

The following questions might guide you through the advice:

- How would you characterise the market?
- What are the segmentation criteria you would apply?
- What are the segments you would opt for?
- What would be your strategy regarding
  - Product
  - Distribution
  - Promotion
  - Price

**Case F            Strategic mix**

Sam wants to start a medium sized bakery. Sam is a friend of the family and so your advice is being asked: you have participated in a sub sector study didn't you?

What is the advice you can give to Sam? No further information is provided since you buy bread and cakes so the information is known. *In case you are missing information: you state that you miss that information and you assume certain facts.* In principle everything is possible, as long as you can reason your argumentation!

The following questions might guide you through the advice:

- How would you characterise the market?
- What are the segmentation criteria you would apply?
- What are the segments you would opt for?
- What would be your strategy regarding:
  - Product
  - Distribution
  - Promotion
  - Price

## **2.2 Interview Techniques**

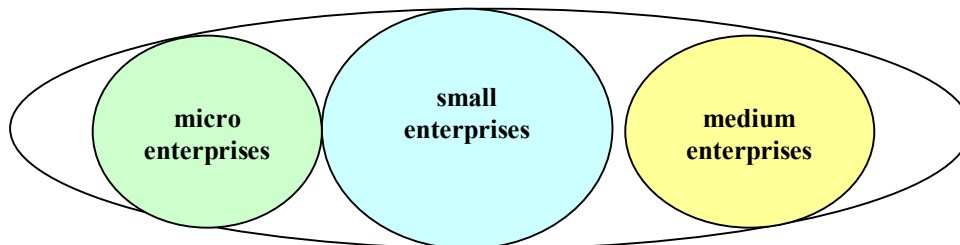
## 2.2 Interview techniques

### 2.2.1 Introduction

When we want to study the sub sector, we should read as much as we can about the sub sector: we should look for documents and articles that might have valuable information for us: we call information we received through such sources secondary information. But, no matter what, we shall have to obtain primary information: information from the field! That means we will have to talk, to interview, the main actors in the sub sector.

### 2.2.2 Who to interview

It is important that we select a good sample of the SMEs. The aim is to get maximum information through a minimal number of interviews. If our main focus point is the small enterprise, we should spend half our time with that target group, leaving one quarter of the time with enterprises on the left (micro enterprises) and one quarter on the right (medium enterprises).



*Why do we need to talk to these other enterprises if they are not our target?*

These entrepreneurs are working in the same sub sector and they can give us a lot of information about the sub sector itself. Often they are buying from or selling to these companies, sometimes they are competing with these enterprises. The information we will get from them about the sub sector and the small enterprises in general is information we will not easily get from the small enterprises themselves.

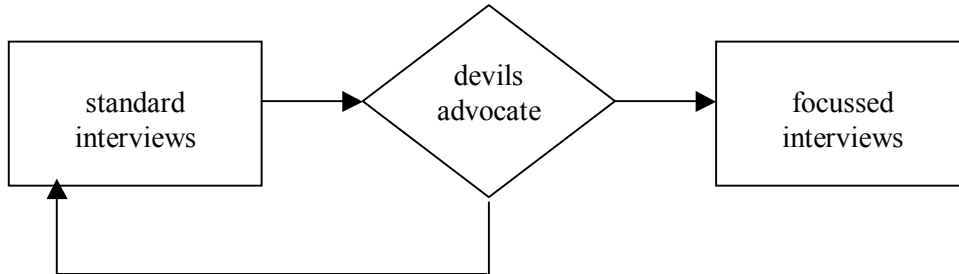
*How many interviews will we do?*

This is difficult to predict: it depends on the complexity of the sub sector, the number of actors in that sub sector, and how quick we get the required information. It also depends on the quality of the selection of enterprises, the interviews themselves and a little bit of luck! Often this implies that we have to interview some 15 to 20 enterprises.

Once we get “the feeling” that we have a reliable picture of the enterprises we have done enough interviews. This point is reached when we “get the same answers” to our questions. However, we should be careful: we might be asking the wrong questions or we might be “wanting to hear the same answers”.

A good way of checking whether we have a complete picture without question marks or contradictions, is to ask somebody else to play “the devils advocate”. One team member will be charged with asking “tough questions” to which the other team members should respond: if there are some uncomfortable moments, some doubts, some guessing, than we are not yet ready yet.

We will use a standard questionnaire for all the interviews in order to create a reliable database. However, if we feel that we have most of the information but there are certain issues missing, we will undertake some more interviews whereby we focus on these blanks.



### Where to start?

*When you are walking through the desert you will first see trees, once you are near the trees you will see the bushes, and at a close look you will see the sprouts.*

That is one of the reasons we will start with the medium enterprises: they are easiest to locate. Secondly, due to their size and age, they are well informed and often better at explaining and discussing issues about the sub sector. Moreover, they know most other enterprises, also micro producers and through them we will be able to locate other producers.

Since we probably know little about the various types of small enterprises it will be difficult to set criteria in the beginning. Normally with such samples, you set certain criteria that your sample has to meet: male and female, young and old, small and big. In this case, it would be best to keep asking ourselves during the exercise whether the sample is a true reflection. Have we interviewed different enterprises at different locations? So we don't limit ourselves to one neighbourhood or to one market place. If we have interviewed mainly entrepreneurs that are "at age", let us look for some younger entrepreneurs. If they all sell to the same type of customers, let us look if there are others who sell elsewhere.

It would be best if we look at these criteria once in a while (for example at the stage when playing the devil's advocate) and then plan some additional interviews to cover the "left out" enterprises.

### 2.2.4 Subjective information

Entrepreneurs (*well, everybody actually!*) will give their side of the story: information the way they see it. The information is often subjective and hardly objective.

We therefore should talk about facts and not about opinions. So we don't ask:

Q: *Are raw materials cheap or expensive?*  
A: *Yes they are expensive!*

but we ask:

Q: *How much does one kg of seed cost at the market?*  
A: *I paid \$5 last month at the local market in town!*

We should also be aware of hidden agendas:

*John: "I'm not such a skilled craftsmen as I should be, but I'm not going to tell them; let me blame it on the poor quality of the raw materials!"*

Peter: "If I complain a lot about the high cost of raw materials; these NGOs might give these materials for free"

We should also be careful of miscommunication:

Q: *How many people work at your workshop?*  
A: *I pay 3 carpenters and 2 assistants*

If we conclude that there are 5 workers we are wrong: his two sons work there too, as does one nephew who is being trained and is thus not paid, as well as his wife who does all the administration.

Avoid putting the words in his mouth:

Q1: *So it is difficult to find raw materials?*

He will be tempted to agree (in a way) that it is difficult, even if it isn't really a problem.

Q2: *So do you find it difficult or easy to procure raw materials?*

That questions leaves him with a choice: difficult or easy or ....

### 2.2.5 Do's & Don'ts

How would you react if somebody knocks the door and asks you:

*What do you do for a living?*

*Really, are you properly trained for that?*

*How much salary do you get?*

*Is that all you make?*

*How much did you pay for your car*

*That's too much for such an old thing!*

*When did you marry your wife?*

*Because you made her pregnant or what?*

*How often do you cheat on her?*



Well, the entrepreneurs might react in the same way!

So ask yourself; how would you like to be treated and then treat him likewise!

**Inform him about the objective of the interview.** Present yourself, tell him that you are studying the sub sector and that you would like to interview him to get information about the sub sector and his company. Let him know that you are interested in him: he knows a lot and you are there to learn from him. Ask him if he is willing to do so and if he has the time to attend to you now: inform him about the length of the interview and what you will and will not do with the replies. Confidentiality is important. Most interviewees get a bit nervous if they see big questionnaires. Inform him what the subjects and sort of questions are and what you write down. Inform him what will happen with the results and how confidentiality is guaranteed. Be aware that you as a person and as a member of an organisation do have a background that might influence his replies. Your uncle works at the ministry, your organisation has a reputation for assisting the poor,... etc.

**Try to break the ice;** first leave the questionnaire in your bag, talk about some niceties and show interest in his workshop. Many will offer to have look at the workshop first. That will give you the opportunity to see what kind of workshop it is (size, dynamics, products) and while touring might break the ice: be curious, talk to employees, show interest, be impressed (if reason) but given time; keep it short. Don't ask too many questions to the employees (you haven't been talking to the owner yet!) but it will give you a hint about hierarchy, norms and attitudes.

**Show respect** even if he is not very cooperative. That doesn't imply that you have to agree to whatever he says, you may be confronting sometimes but you should avoid a debate or a confrontation: you are there to absorb as much information as possible. Once you are arguing he will not give you all the correct information!

Always confirm the answers: the entrepreneurs might use many words to explain a certain issue, after listening to it, try to summarize it in a few words and check whether that is the correct conclusion.

**Try to find a balance** between asking all the questions on the questionnaire and maintaining a conversation. If we ask the questions 'the way they are written' than the interview becomes more like a cross-examination. Rephrase them so that they sound natural. If we only chat and go from one issue to another like a butterfly we probably end up with a lot of blanks. It should be a dialogue whereby the questionnaire provides the structure.

There is nothing so depressing when the interviewee has mentioned certain facts earlier and the interviewer asks questions about the same facts as if he never has heard about them. So in case you come up to already answered questions, skip them, or if you need more information, confirm what you have heard earlier and ask additional questions.

Asking questions is one source of information, **using your eyes** is another:

*“My equipment is very old”* - *seeing a brand new shining machine*  
*“I have 30 customers per day”* - *there was no customer while you were there*

When having asked all the questions you wanted to ask, ask him if he has some questions for you! Most likely these questions will be about the next step: what will you do and when will he hear from you again? **Inform him about the next steps** and confirm once more that he will be invited for a feedback workshop where the preliminary results will be discussed.

## 2.2.6 The interview

### The questionnaire

In section 2.2.7 there is an example of a questionnaire that can be used for enterprises. However, this questionnaire is designed for use in all sectors and is therefore rather extensive but also rather general and needs to be adjusted by you for your sub sector.

In principle we want to get information about:

- his market; his clients, the procedures, the size, the segments, the prices
- his procurements; his basic materials, his suppliers, the procedures, the costs,
- his production; the process, the labour, the machinery,
- his financial situation; the income, the expenses, the investments,

And so we ask:

- what .....
- where .....
- when .....
- why .....
- who .....
- how .....

We have to remember that we will hear about facts and opinions and that we have to distinguish between the two! We will be tempted to ask too many questions: some will not be that relevant, others will be crucial and require more time. But time is limited: we are ‘stealing his time’ and so we must limit the length of the interview: one interview should not last longer than one hour.

At the end of the interview ask him to mention the main problems he faces. Mark them in the fields according to the entrepreneurs importance. Thereafter, mention the possible problems and ask him to state whether they are a problem or not. This way we will be able to list the main problems without influencing the entrepreneur.



## Teamwork

It would be best if we would do the interview with two persons. Two persons hear and see more than one person, it allows one to exchange views and it is practical. One person could focus on the actual questioning and the other person could focus on making notes. This implies you will work as a team and that will require some practising! The biggest advantage is that you will be able to do an analysis right after the interview! (there is always a shady tree around and you don't need a table). Within half an hour discuss whether:

- All the questions have been answered
- The answers are understood and make sense
- There are some blanks or doubts
- You heard facts, opinions or rumours
- The interview itself was satisfactory
- Write down the most important conclusions ( on the last sheet)

## 2.2.7 Standard questionnaire example

Date:	Interviewee:
Interviewer:	Sector/Activity:
Code:	Locality/Neighbourhood: POBox: Tel.:

<b>General</b>	
Function of interviewee	
Date of establishment enterprise	
Age of the enterprise	

Workers	owner	master	helpers	apprentices	Total
Total					
Number of women					
Number of men					

<b>Legislation</b>	
What type of registration do you have? (documents)	
How much time did that take? <i>Difficult or easy? Did you pay? (formal or informal)?</i>	

<b>Products</b>	
On order or for stock? <i>(in order from most to less products)</i>	
	Last year price      Present price
1.	
2.	
3.	
4.	
5.	
<i>why? how? tendencies? New products or the same? Designs?.....</i>	

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<b>Clients</b>			
Origin of the clients? <i>neighbourhood, town, outside, ...</i> <i>(try to quantify (%..))</i>			
Intermediaries or consumers?			
Frequent or occasional?			
What do you do to draw clients?			
<i>Number of clients</i> <i>(for each group of clients/segment)</i>	last year	this year	
1..			
2...			
3....			

<b>Competition</b>			
Do you have competitors? Who? <i>name, address, locality,..</i>			
1..			
2...			
3....			
Why do clients buy from you ( <i>your strong points in relation to your competitors</i> )			
<i>why? how? tendencies? changes?</i>			

<b>The market in general</b>			
What are the tendencies you notice?			
The supply is increasing or decreasing?			
The demand is increasing or decreasing?			
Is there competition from imported products?			
<i>why? how? tendencies?</i>			
Threats			
Opportunities			

CAPSA

<b>Basic material</b>			
<i>(in order of importance)</i>	last year	this year	
1.			
2.			
3.			
4.			
5.			
Suppliers of:	volume	address / locality	
1.			
2.			
3.			
4.			
5.			
<i>why? how? tendencies?</i>			

<b>Machinery and equipment</b>			
<i>(in order of importance)</i>	previous price	actual price	origin/age
1.			
2.			
3.			
4.			
5.			
Are the machines adequate or not?			
<i>Tendencies? Observations?</i>			

<b>Financial aspects</b>	
What were the major investments?	
What is the value of your stock in basic materials?	
What is the value of your stock in final products?	
What is your actual capital? <i>(price of everything, at sales value)</i>	
Did you have access to credit? <i>For what purpose, where, conditions, interest rates, guarantees, process....</i>	
How are your sales paid? <i>(cash on delivery, in advance, on credit)</i>	
How do you pay your suppliers? <i>(cash on delivery, in advance, on credit)</i>	

CAPSA

<b>Revenues</b>			
Revenues per month	minimum	maximum	average
Which are the months with minimum sales?			
Which are the months with maximum sales?			
Is it increasing or decreasing?			
<i>Why? How? And in the future? Other incomes from ...?</i>			

<b>Services</b>	
What services do you receive / need? <i>Tel., waste, electricity, garbage collection, etc.</i>	
Problems? <i>Cuts, costs?</i>	

<b>Identification of problems</b>		
<i>Ask what his/her main problems are. First ask what his/her problems are without mentioning the possible areas and mark them as X in the first column and thereafter mark X in the second column when you mentioned possible areas (options).</i>		
What are the problems you face ( <i>number</i> )	without mentioning	when mentioning
lack of capital		
lack of clients		
lack of tools and or machinery		
lack of basic material		
lack of qualified personnel		
lack technical knowledge		
problems with licences and or other documents		
other problems such as .....		

CAPSA

**Evaluation:** *After the interview, review all answers and information obtained and discuss it!!!  
Thereafter, write down the main conclusions and information.*

Products	
Clients	
Market	
Basic material	
Machinery	
Financial Aspects	
Observations	
Special information	
1	1
2	2
3	3

## **Tasks Unit 2**

## Tasks Unit 2

### 1 We haven't interviewed the producer yet, but what are your thoughts about the following aspects? Discuss them and write them up!

- The characterisation of the market.
- The segmentation criteria.
- The possible market segments.
- The possible strategies in relation to:

Product  
Distribution  
Promotion  
Price

### 2 The standard questionnaire needs to be revised to suite our sub sector:

- What are the questions in the standard questionnaire that are not relevant for our sub sector.
- What are the important issues or questions that are important for our sub sector but that are not included in the standard questionnaire.
- Prepare an appropriate questionnaire for your sub sector.

### 3 The sample of entrepreneurs that will be interviewed is very important:

- Define the selection criteria.
- Develop a practical plan to hold the interviews that includes a test-run.
- Interview!



## **3 Maps**

## **3.1 Data Base**

### 3.1 Data base

#### 3.1.1 Introduction

The findings of the interviews need to be analysed. A database will assist us in drawing conclusions. A database does not draw conclusions for us. A database is no more and no less than a file where we store information in such a way that we obtain summarized information. However, the quality of the information we draw from the database depends on the quality of the information that we put in to the database. Have look at the following database that shows us how much money 15 participants have at their bank account:

	<b>Number participants</b>	<b>Score</b>	<b>Total</b>
	1	100	100
	1	1000	1000
	2	200	400
	3	175	525
	4	150	600
	5	125	625
<b>Total</b>	<b>15</b>		<b>3250</b>
Average			216,67

At a first glance we see that the average equals 216,67 and if not questioned, that figure might enter our analysis. Yet, we see one huge distortion: one participant (number 2) has much more on his bank account than the other 14 persons. There are two possibilities: he is a real exception (and then we must find out why!) or, as we found out when checking the questionnaire: we entered one zero too much!

So you must be careful when processing. The mistake or exception would have shown much easier had we ordered the scores in a different way:

	<b>Score</b>	<b>Number participants</b>	<b>Total</b>
	100	1	100
	125	5	600
	150	4	600
	175	3	525
	200	2	400
	1000	1	1000
<b>Total</b>		<b>15</b>	<b>3250</b>
Average			216,67

The mistake in the above example is quite obvious, yet, when we receive information about our interviewees, we must also assess that information before we enter it in our database. Suppose that 5 out of 15 participants did not reply honestly. If we do enter the false information in the database, the average figure (with two digits behind the dot!) becomes a reality after some time: we will not question the information and we take it as a fact. We therefore must be sure we enter only true and correct information in the database (the five had only \$10 on their account; the average dropped from 217 to 133!)

We also must be careful that we only enter data that we can use in our analysis! Suppose we were to check how much income these participants had: does the information provided (bank accounts and averages) give us any clue?

Therefore we must always remember that: **garbage in = garbage out**

### 3.1.2 Information

After completing the interviews, we will have three sorts of information:

- Facts        such as the price of raw materials, the number of workers
- Opinions   such as raw materials are expensive, that workers are difficult to find
- Rumours    that a foreign company might take over another company

We also have two types of information:

- figures
- words

Both *facts* and *opinions* enter our database, but we have to treat them differently: the first is objective information while the second is subjective information. We should not mix the two, but both types of information are valuable. *Rumours* don't enter our database; we can't add and average rumours! However, these rumours might become facts if verification proves them true.

*Numbers* are easiest to enter and to use in a database since we can apply mathematical rules to them. We should not attempt to apply these rules to *words* but we might enter them, since the simple fact that they are there, can provide additional information.

The risk with numbers and databases is that they start living their own life and we must never forget that although the database may assist us, *it will not do the analysis for us*. It is therefore best that we also do a qualitative assessment (databases are always quantitative) where we combine the two!

Given the fact that the number of questionnaires is limited, there is no need to design fancy but also complicated databases that can play tricks with our entries! A simple sheet and a pen are sufficient for our database (although there is no objection to use an excel spreadsheet which is not much more than a digital piece of paper combined with a calculator). There are three basic rules:

- it must be easy to enter data with minimal risk of wrong entries or manipulations
- it must be easy to manage and maintain the database
- it must be easy to draw (summarised) data with minimal risk of mistakes

### 3.1.3 Numbers

Looking at the first question of the standard questionnaire we could think of the following database:

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	T	A
<b>Owner</b>	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	15	1
<b>Master</b>	1	2	0	5	0	0	2	0	1	0	3	2	6	0	5	27	2
<b>Helpers</b>	1	3	0	6	2	1	1	0	2	3	5	5	13	0	4	46	3
<b>Apprentices</b>	0	1	0	3	2	0	1	0	0	0	2	1	5	0	0	15	1
<b>Total</b>	3	7	1	15	5	2	5	1	4	4	11	9	25	1	10	103	7

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	T	%
<b>Male</b>	3	7	1	11	5	2	5	1	4	4	7	9	20	1	10	90	87
<b>Female</b>	0	0	0	4	0	0	0	0	0	0	4	0	5	0	0	13	13
																103	100

The respondents are numbered and listed on the top row. The scores are simply entered the way they were in the questionnaire. In the last two columns we have entered the totals per row and the average per row. By colouring the maximum (blue) and minimum (red) scores per row we see them at one glance.

We can easily make some additional notes: apprentices are only employed by the larger firms that employ more than 5 workers. The relationship between masters and helpers is roughly 2:3 and that with the exception of 3 micro entrepreneurs, they always employ helpers.

We also note that there are only 13% females employed (we don't know in which capacity - that wasn't asked) and that these ladies are employed in 3 companies only, also being the three biggest among them!

### 3.1.4 Words

If we look at the question about the clients, we see that the replies are words and not numbers. This makes it difficult to compare and draw conclusions, and we have to depend much more on our creativeness and logic! The following example appears complicated: take your time and try to follow the reasoning.

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	T	A
<b>Origin</b>	N	T	?	O	T	N	T	?	N	N	OT	T	OT	N	T		
<b>Type of clients</b>	C	C	C	I	C	C	C	C	C	C	I	C	IC	C	IC		
<b>Frequency</b>	O	O	O	F	OF	O	O	O	O	O	F	O	F	O	F		
<b>What do you do?</b>	N	N	N	C1	C2	N	?	?	C1	N	C1	N	C2	?	?		
<b>Total</b>																	

We have coded the replies: Neighbourhood (N), Town (T) and Outside (O) for the origin of the customers, the type of clients we have coded Intermediaries (I) and Consumers (C). The same we have done for frequency: Occasional (O) and Frequent (F). For the type of marketing this is a bit more complicated: most do nothing at all (N) while others do something: C1 means they have simple leaflets and C2 means they have local advertisements. If we don't have a reply, we put a question mark.

Note that we cannot add scores and provide averages. In this case we have to draw conclusions using our logic! Five companies produce for the neighbourhoods, all of them consumers that buy occasionally and they do nothing in terms of marketing except one. There are 3 companies whose customers are mainly from outside, most of them intermediaries that buy frequently and all three companies do something about marketing. The third group produces for the town, except one all for consumers, few occasional and few frequent, and little can be said about their marketing: a few question marks, a few do and a few don't.

It is important that we give each respondent an identification number (in this case 1,2,3 etc.) since this is the only way in which we can draw more conclusions: we see that the three biggest companies (numbers 4, 11 and 13) are the companies that produce mainly for outside and we might suspect a relationship there: if you grow you can produce for foreign markets OR if you produce for foreign markets you will grow!

The latter shows us how important the qualitative analysis is: a database does not provide us with an analysis; it only assists us by storing the data in such a way that we may see these relationships.

### 3.1.5 Categories

Since we may have some doubts on the accurateness of the replies we may also use classes rather than the actual replies: not only do we avoid a certain accurateness that is not correct, it is also easier to oversee the replies and draw conclusions. Let us have a look at a reply to the question how many customers they have per month:

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	T	A
<b>Clients / month</b>	3	5	2	7	4	2	8	5	1	6	3	9	9	4	7	75	3

Conclusions are not that easy to draw: the average is 3, the lowest has 1 and the highest have 9 customers.

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	T	A
<b>Clients / month</b>	A	B	A	C	B	A	C	B	A	B	A	C	C	B	C	75	3

When we classify the replies in three categories A= 1-3, B= 4-6 and C= 7-9 we see that five enterprises have around 8 customers, four enterprises less than 3 and six enterprises between 4 and 6 customers per month. We could also apply such classifications for “words” e.g. very difficult – difficult – easy – very easy.

### 3.1.6 Various databases

We should be careful what information we do combine and what information we do not combine in one database. Since we are talking about few respondents we can combine e.g. the micro, small and medium enterprises: it will actually show what are the differences between the three, if any. However, we should not mix the enterprises with other respondents that we will interview: suppliers, key informants and the various customers.

Hereafter an example of a data base (based upon the standard questionnaire) is presented.

- Design an appropriate database to process your questionnaires
- Enter all the collected data in the database

## 3.1.7 Standard database example

Date:	Interviewer:	Sector/Activity:	Code:
-------	--------------	------------------	-------

<b>Enterprise number &amp; name</b>	1 .....	2 .....	3 .....	4 .....	5 .....
locality					
age owner					
age enterprise					
educational level					
professional education					

<b>Workers</b>					
totals					
- women					
- men					

<b>Legislation</b>					
type of documents					
difficult or not					
how much paid					
where paid					

<b>Revenues per month (average)</b>					
2001					
2002					
2003					

<b>Products</b>					
on order or for stock					
1					
2					
3					

<b>Products</b>					
prices increase or decrease (%)					

<b>Clients</b>					
number of clients					
number of competitors					
intermediaries / consumers					
competition imports y/n					

<b>Market in general</b>					
supply increased / decreased					
demand increase / decreased					
competition imports					

<b>Basic material (price)</b>					
basic material					
increase or decrease (%)					
others					
increase or decrease (%)					



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<b>Basic material (supplier)</b>					
volume / year basic material					
number of suppliers					
other costs					

<b>Machinery</b>					
value of machinery (historical)					
value of machinery (actual)					
state/condition					
problems/lacking machinery					

<b>Personnel</b>					
masters					
others					
problems yes/no					
salary (average)					

<b>Financial aspects</b>					
initial capital					
Actual capital					
stock value (basic material)					
value of final products in stock					
bank account					
bookkeeping					

<b>Services</b>					
electricity; problems y/n					
others; problems y/n					

<b>Networks</b>					
member y/n					
Subcontracting y/n					

<b>Problems (indicial)</b>					
lack of capital					
lack of clients					
lack of tools and or machinery					
lack of basic material					
lack of qualified personnel					
lack technical knowledge					
problems with licences etc.					
others .....					

<b>Problems (mentioned)</b>					
lack of capital					
lack of clients					
lack of tools and or machinery					
lack of basic material					
lack of qualified personnel					
lack technical knowledge					
problems with licences etc.					
others .....					

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Products	
Clients	
Markets	
Basic material	
Machinery	
Financial aspects	
Observations	
Special information	
Positive	Negative

## **3.2 Mapping Tools**

## 3.2 Mapping tools

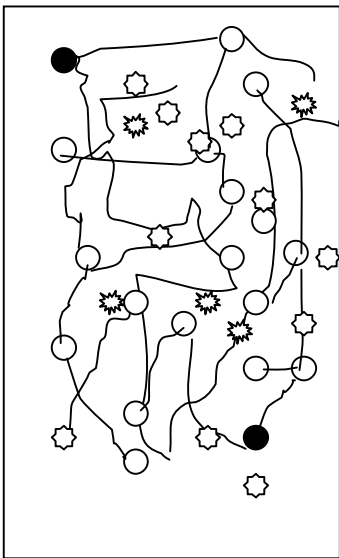
### 3.2.1 Introduction

*How does one explain to somebody how to get from A to B? What is the easiest way to show somebody an area unknown to him? One describes, one shows pictures, one makes maps....*

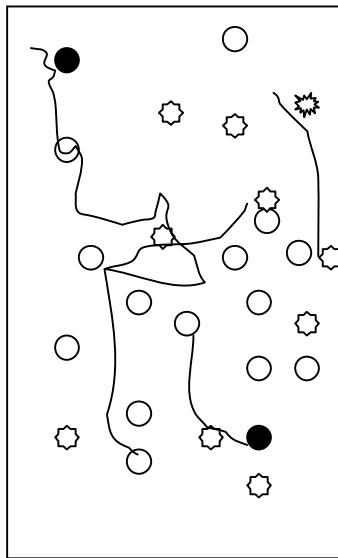
In this way we shall also try to make a picture of the sub sectors: we look at the sub sector and the actors, and we sketch how they are linked to each other. The main red line is the flow of the products; how do they go from one to another; from raw materials, through assemblies, sales up to the consumption by the customers. Like we mentioned before, the basis for the analysis is to look at the flow of the raw material.

*The trick is to find a balance between insufficient and too much information.*

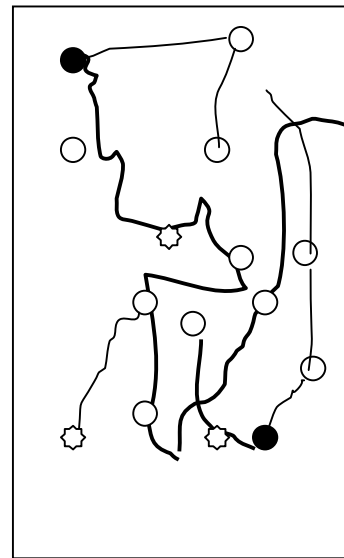
The roadmap on the left side has so much information that we need to puzzle our way between the two dots: there are so many signs we can't read them anymore. The second road map doesn't have enough information: we can't find our way between the two dots: vital information is missing. Only the third map on the right tells us at one glance how to get from one dot to the other!



too much



too little

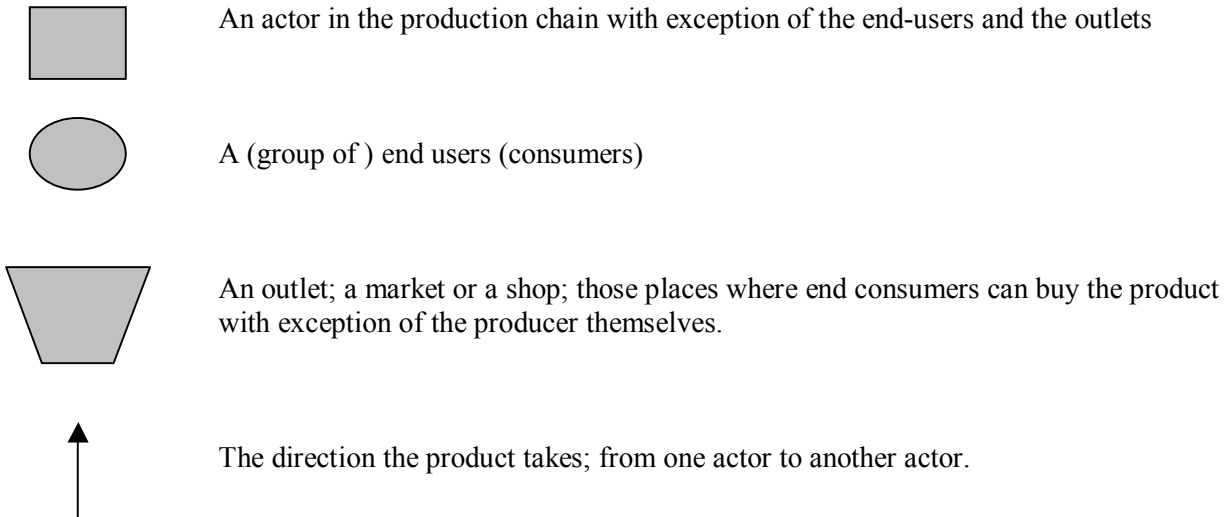


OK

### 3.2.2 Sign language

We must also agree / know what the signs mean: in the roadmaps we agreed that the circles / dots are towns or villages, the lines are the roads and the stars are landmarks. If one doesn't know the latter, one might as well think that the stars are bars, mines or hills.

So let us first agree on the signs we will use for our maps:



The above symbols are for the actors; we also have to agree about the layout: as with a roadmap; the north is always at the top. We start at the bottom of the chain and thus at the bottom of our map and work our way upwards towards the end-users. For easy reference we divide the map in 5 principle areas:

- consuming

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- retailing

---

- wholesaling

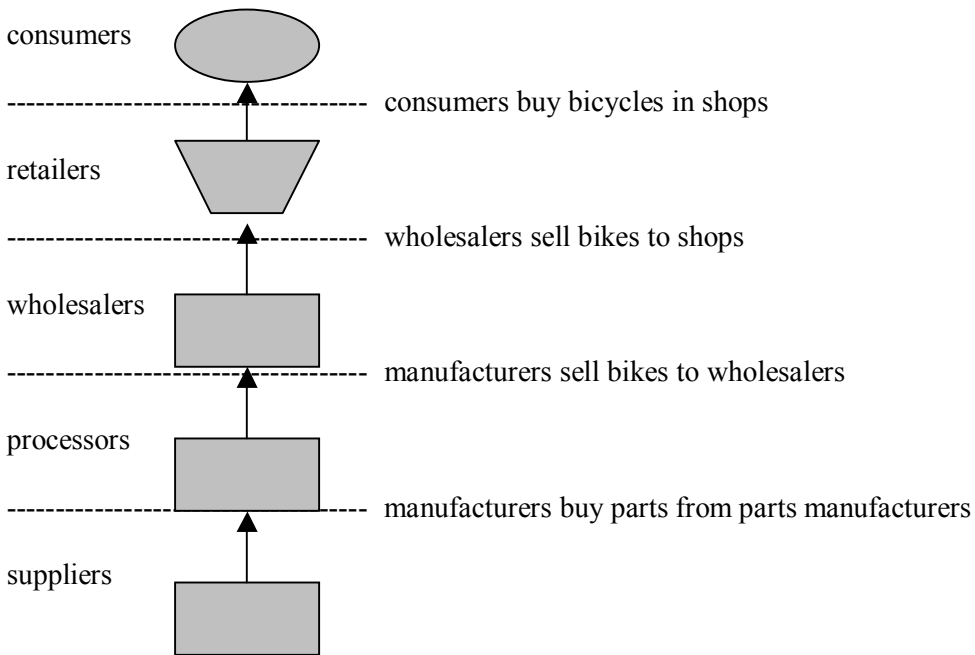
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- processing

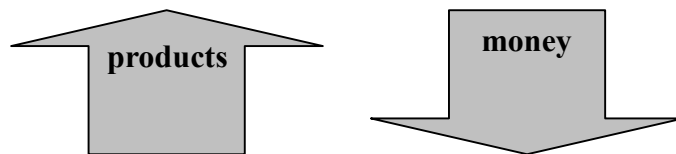
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- supplying

**A basic map looks like this:**



There are of course no standard maps; every sub sector has its own characteristics and ways of production and so the maps differ (they might even differ in time!). The only certainty is that products go up and money goes down!



### 3.2.3 Various forms

What are the most common variations or alternative channels?

- **More actors in between:**

- Where would you place a trader who buys tomatoes from farmers and sells them to factories that make tomato juice?

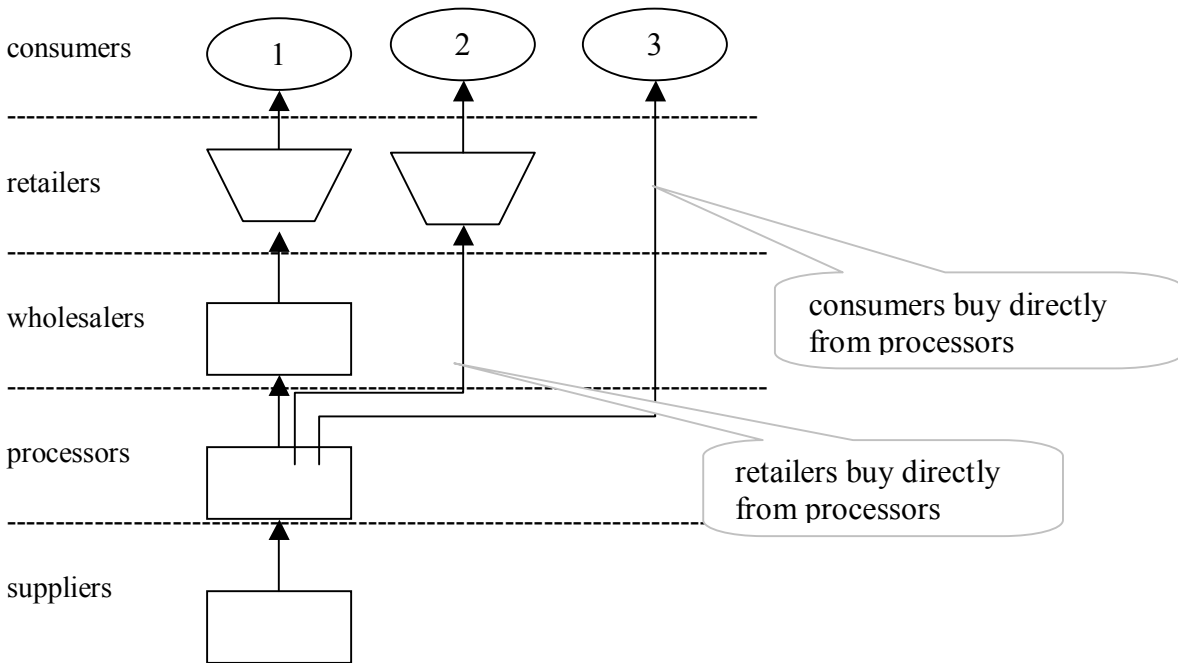
*In the supplier section; between suppliers and processors.*

- Where would you put street vendors that buy bracelets from shops?

*In the retail section: between shops and consumers.*

- **Different paths:**

If there are more paths from the processors to (different) consumers we simply add more channels:



In the above picture we have sketched three channels:

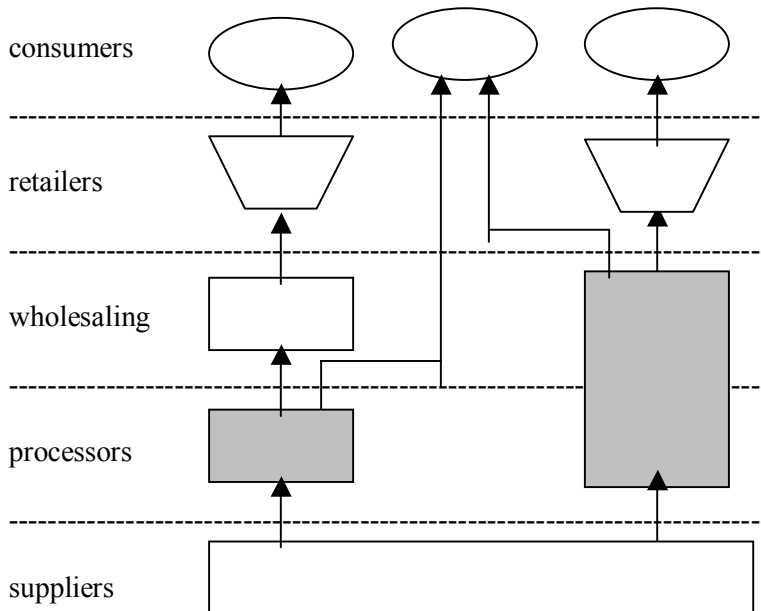
- 1 producers sell to a few wholesale companies in town. Rural retailers come to town and buy from these wholesalers to sell it to their rural clients.
- 2 urban retailers buy directly from the producers and they sell these bikes to the public in general
- 3 consumers in the neighbourhoods of the producers buy their bikes directly from the producer.

The map tells us that:

- 1 all producers use the three channels
- 2 the consumers have different characteristics (segmentation criterion = geographical location!)

- **Different paths for different producers**

What if there would be a few producers who sell to the wholesalers only and a few other producers who sell to retailers only: their marketing channels differ and we should use the following map:

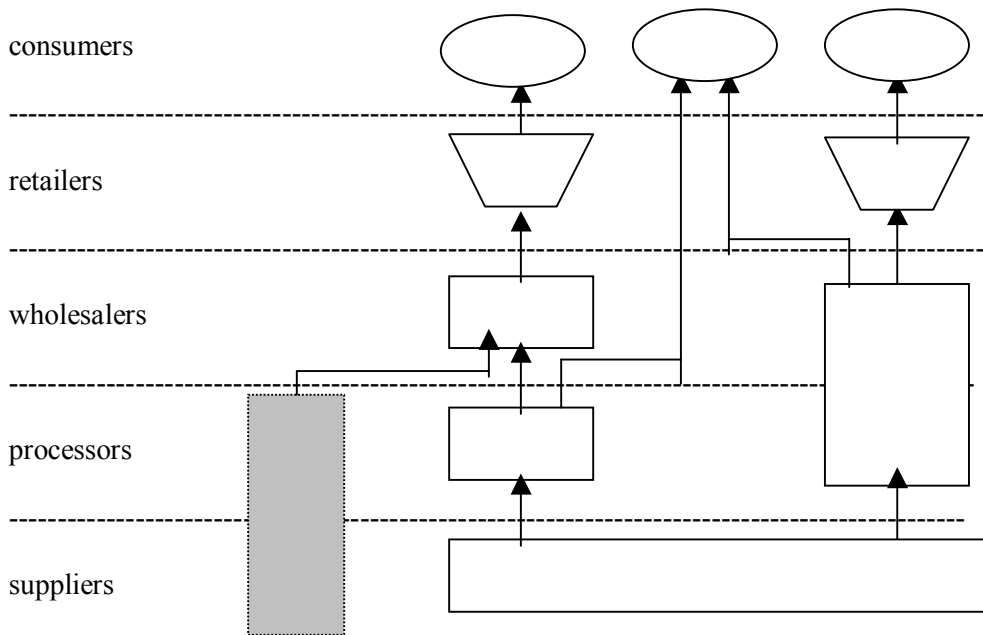


The producers on the right side sell directly to the shops while the producers on the left side sell to the wholesalers only. They have different channels, different numbers of customers, different volumes per sales, different prices and different margins. That is the reason that we separate between the two types of producers!

More often than not, they are also different types of producers; e.g. the small/medium producers sell to wholesalers all over the country while the micro/small producers sell to shops in their own town. In this case don't think that the right side producer is bigger: the size on the drawing only indicates that he performs two functions: producing and wholesaling (selling directly to retailers)



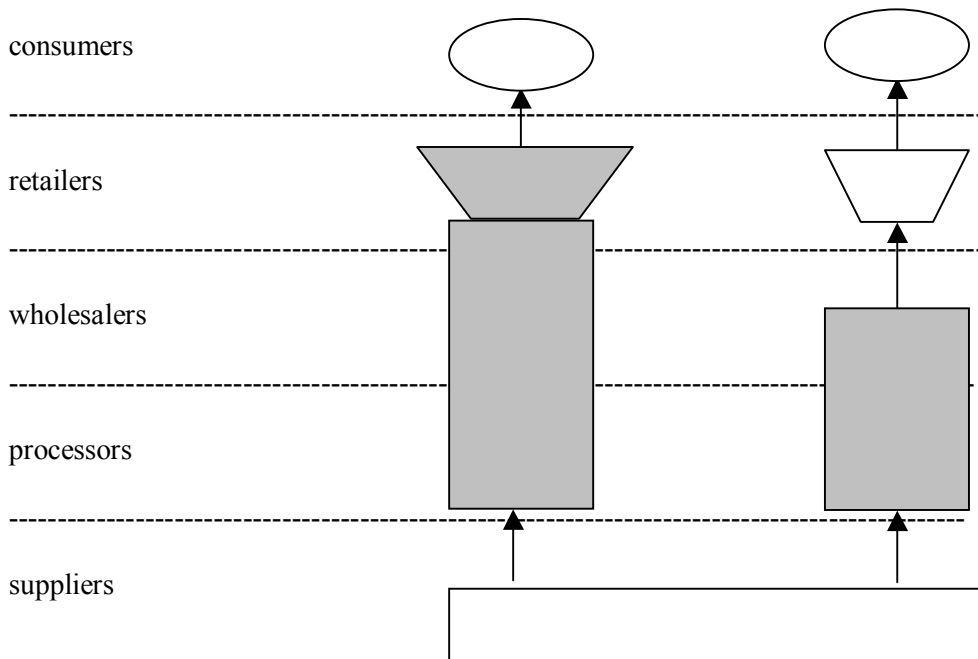
- Importing channels



You can imagine that wholesalers also import bikes from neighbouring countries; in that case the whole production process takes place elsewhere and the bikes enter at the same point as the bikes from the local producers. In that case it would be good to use dotted lines (*we don't know and don't care how the process works in neighbouring countries*) to separate the flow from the other production flows.

*So you see how complicated the map tends to be: therefore we must be very strict about the signs: all the arrows go from the top of one actor to the bottom of the next actor; if we would allow to enter from the side or downwards, the map becomes too difficult to read.*

- **Producers with different functions**



The producer on the right side produces bikes and sells them (in larger quantities probably) to shops; he focuses on the production.

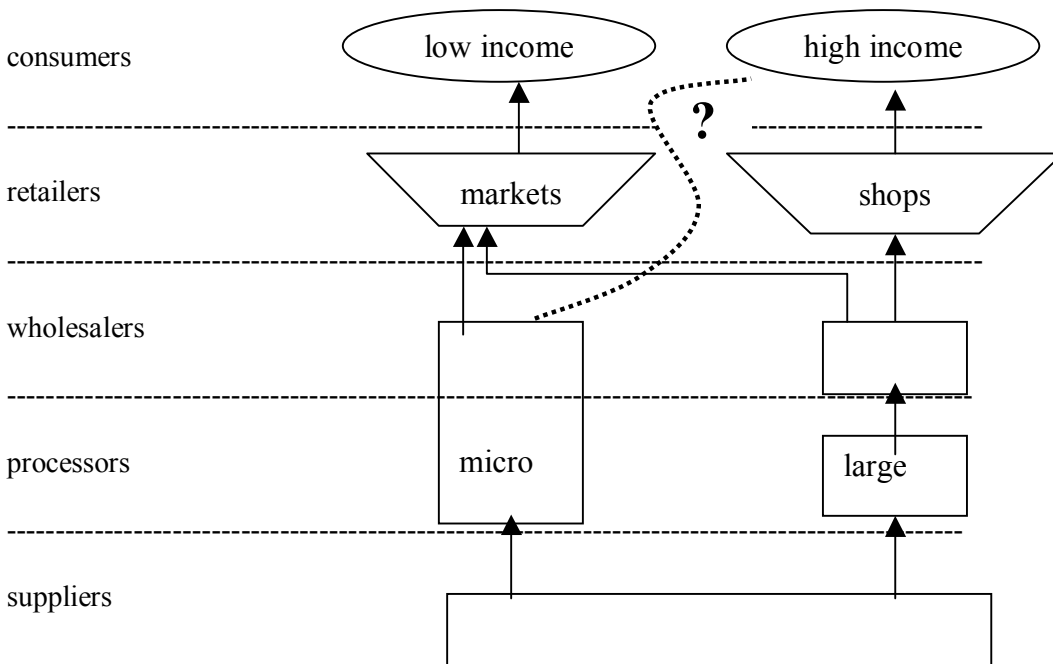
The producer on the left side produces bikes but he himself also sells to the public; e.g. he has a workshop and in the front of that workshop he has a little shop where his salesman sells to individual customers; his sales activities are than just as important as his production activities! In that case we combine both symbols!

The producer who produces and sells does not only have a larger gross profit margin (higher sales prices) but he is close to his end-consumers: he knows them, he knows what they want, he knows what they complain about: he can react to the market! He can also render other services, such as repairs or advice, which is much more complicated with the other producer because there are two actors in between him and the customer.

*As mentioned before, it is important to make an inventory of all actors and channels and not to focus only on our defined target group. Because the other actors are influencing the micro and small producers, we have to draw a complete picture.*

### 3.2.4 Segmentation of the market

The segmentation of the consumers is another very important aspect for our mapping exercise. Very often we see that certain groups of consumers buy from certain (types of) producers while other groups of consumers buy from other (types of) producers. Using segmentation criteria will help you draw the map, while drawing the map will help you to determine segmentation criteria; an iterative process!



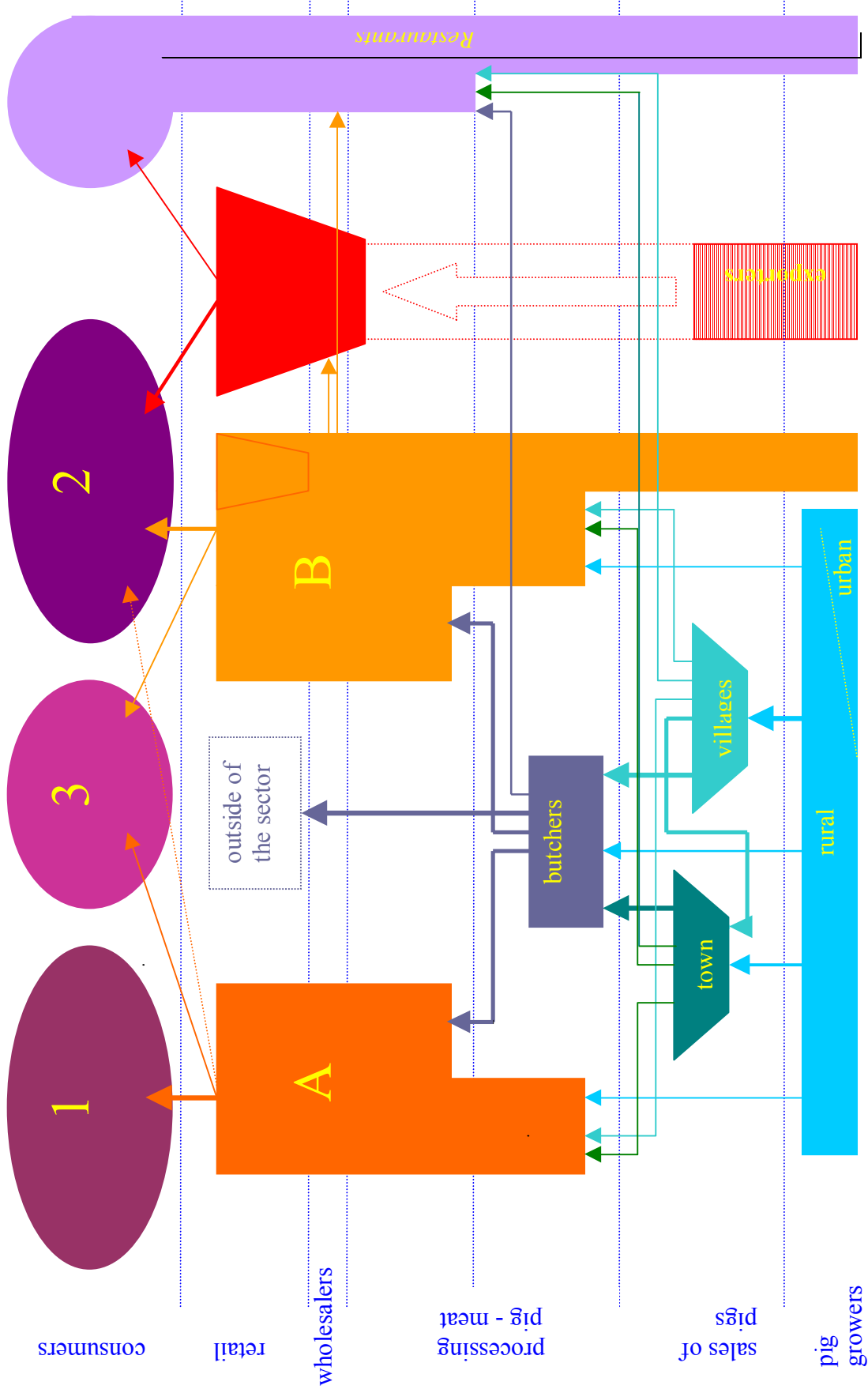
We see that the large producers, through their wholesalers, have access to both the high and low income consumers:

- Marketers buy bikes from wholesalers and sell them, probably without much service and competing on price.
- The shops sell to the higher income groups who either buy the more expensive bikes (quality, design) or they are simply willing to pay more to shops (guarantee, service, finance).

The micro producers produce for the low income group and have to compete on price with the larger producers: probably quite a tough job, while their bikes might even be of a higher quality than those from the larger producer. The link between the micro producer and an attractive segment seems missing.

- How could the producers make that link? Through markets or through shops?
- Which strategy would you advise the micro producers?
- Look at the map in Case A and answer the questions!
- Look at the description in Case B and make the map!

**Case A** Below you see the map that was made by a study team who made an analysis of the sausage sector in one town  
 Look at the map and answer the questions!



**Look at the sausage map and answer the questions**

- 1 From which two sources can town based pig traders buy their pigs?
- 2 From which sources can the butchers buy their pigs?
- 3 What is the difference between A and B in terms of functions?
- 4 What type of customers do butchers have?
- 5 How are restaurants supplied with sausages?
- 6 Where can shops buy their sausages?
- 7 Are there wholesale companies involved in the sector?
- 8 What would the little symbol in B processors mean?
- 9 Where can consumers buy their sausages?
- 10 Could you reason what the characteristics of group 1 and 2 might be using the segmentation criteria?
- 11 What is the longest route of the inputs (meat-sausage) that the customer eats in the restaurants?
- 12 What is the shortest route?
- 13 What are the pros and cons of both channels?

**Case B Furniture makers**

- Read the following description of these furniture makers.

In one rural province there are three types of furniture makers:

1. Micro producers who sell their furniture to one and the same furniture trader
2. Small workshops who sell their furniture to rural and individual clients
3. The furniture trader who buys furniture from producers but also produces furniture

The furniture trader sells his furniture to three groups: local individual clients, the local institutions and to retailers in the urban areas who sell to the urban population.

The micro producers buy their timber from local pit sawyers, the small workshops buy from both local pit sawyers and from a logging company while the big company buys its timber from logging companies.

The pit sawyers sell timber to the mentioned producers and to the public in general (for the construction of houses etc.) and the logging company exports the timber to neighbouring countries. The logging company sells seasoned timber.

- Draw the map
- Answer the following questions:

- 1 What might be a serious risk for the micro producers?
- 2 What is a risk for the major company?
- 3 What might be a strategy that the major company might have therefore taken?
- 4 Where might the local competition be fierce?
- 5 If the local competition is too fierce, the market too limited, what might be an option for small companies?

## **3.3 Sources**

### 3.3 Sources

We have done most of the interviews with the SMEs. We have processed their answers in the database. We have drawn a map of our sub sector. In most cases, there will be some blanks in the map and we have to search for answers! This chapter explains how.

#### 3.3.1 The blanks in the map

There will be different types of blanks and we search for answers in various ways

##### 1. Additional interviews with *SMEs*

Some of the blanks in our map shall have to be taken care off by additional and focussed interviews with some SMEs. We should receive reliable information about ‘the way things are’ according to the SMEs. For these types of blanks we have two options:

- We look for other SMEs in order to obtain sufficient “mass” for our conclusions
- We re-visit some of the SMEs in order to discuss a few specific issues

Which of the two options is most appropriate depends on the blanks in your sub sector map, but the result should be that you are certain about the functioning of the SMEs in this sub sector.

##### 2. Then there are blanks that probably require interviews with other actors in the chain:

- The supply side of the SMEs: the bottom part of the map

What are the constraints ‘down under’: most likely the SMEs will be able to inform you about their suppliers, but they will have difficulty in describing objectively what the problems of the supplier are. They will also not be able to fill you in on the suppliers-of-the-suppliers and it will therefore be necessary to interview these *suppliers*.

- The market side of the SMEs: the topside of the map

We have obtained information about the clients of the SMEs, but we should also talk directly to these *customers* to measure their satisfaction. Their opinion about the products of the SMEs will give us more information about market segments, constraints and opportunities.

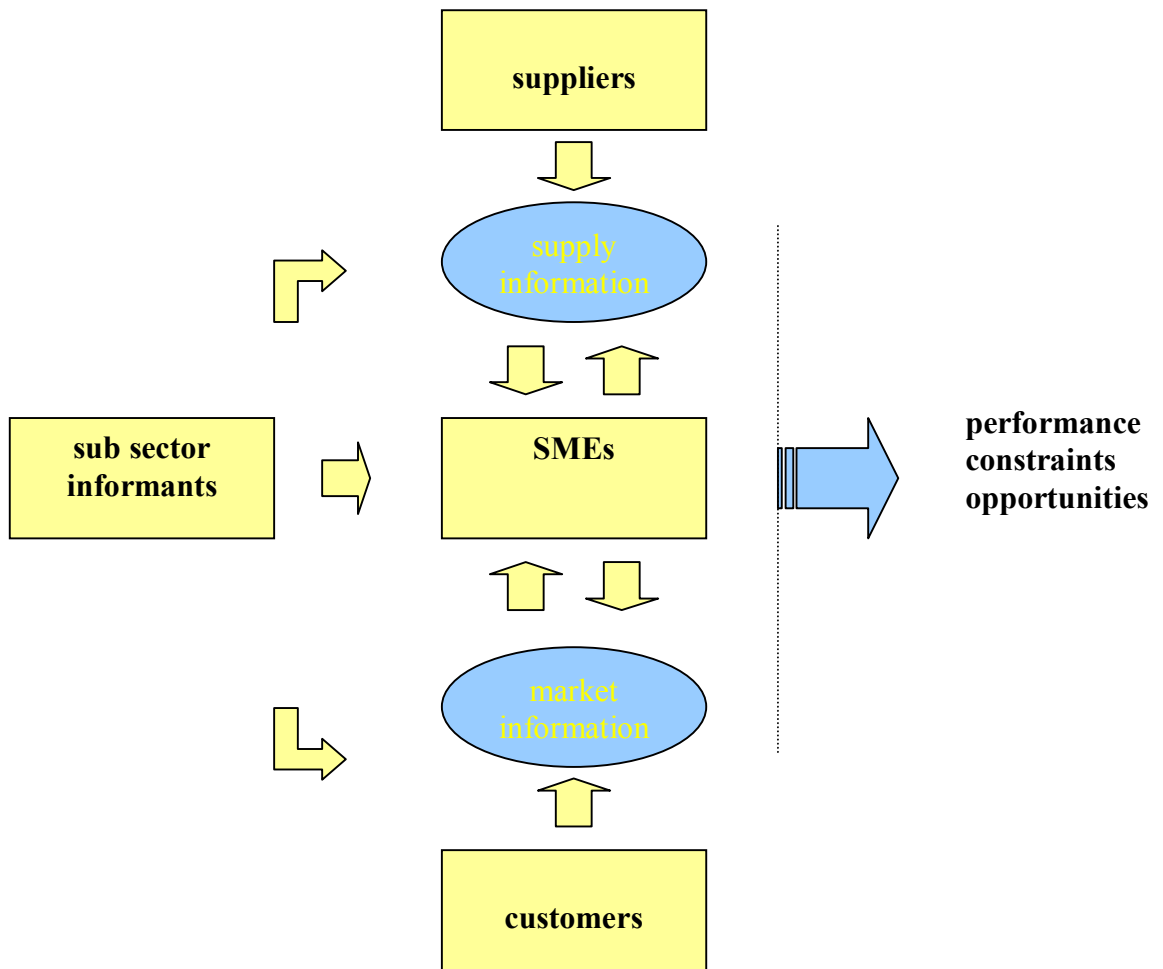
##### 3. Last but not least there are blanks that probably require interviews with *key informants*

The map represents the view and opinions of the SMEs. That is very valuable information, but it is not enough. Their views are not objective because they are actors in the sector: they have an interest! Therefore we must obtain information from other sources too: other actors who are also active in the sub sector but are not SMEs, and key informants who know the sub sector but are not active themselves in that sub sector. The first will provide us with their, also subjective, information while the latter should give us more objective information.

The three types of blanks and sources are visualised in the following schedule. However, before we start looking at the suppliers, consumers and key informants, let us first look at elements that influence the sub sector performance. These elements will also assist us in structuring the next phase.



Sources:



### 3.3.2 The blanks in the environment

Is not our task to only draw a map! If we only draw a map we do nothing more than putting on paper how the sub sector functions, and that by itself does not improve the functioning of the sub sector. We are studying the sub sector so that we can identify constraints and propose interventions that will improve their performance.

The map of the environment for SMEs provided herewith (*last sheet of his unit*) gives us a sort of a checklist of what kind of information is necessary to understand the sub sector.

In the centre we see the sector enterprises and most important issues: the clients they serve, the technology they use, the materials they use, the labour force and the financial aspects related to their functioning.

The “blocks” outside the circle all influence the performance of the SMEs: they put constraints on the market side, they limit their growth or put a burden on their performance in general. We therefore need to research the influence from these “blocks”.

- The policies of the Government are the first block: what does the government do and not do to improve performance, what is their objective, what are their plans?
- The regulations of the governmental institutions: how does one obtain a license, how are taxes collected, how do things work or not work in reality?
- The (semi) governmental services are the third block: how reliable is the electricity supply, how easy can one communicate, how are the roads? Issues that are not specific for our sub sector but do influence its performance!
- The macro economy is the fourth block that provides us with valuable information; is the inflation high or low, how are the exchange rates with the dollars developing, how easy does one change money, what is ‘the cost of money’? All these factors influence the performance of our sub sector!
- The support structures for the SMEs are the fifth block: are there special agencies that provide assistance to the SMES such as NGOs with credit programmes or SME organisations: what are their objectives, how do they function?
- Three minor blocks conclude the map: How does society look upon entrepreneurs? Is there a tradition of trade or production? What is the influence of the climate (farming!) and what is the effect of the sub sector on the environment?

We can now make an inventory of all the information we have gained so far and order it according to these blocks.

- *Make a short summary of key information obtained per block!*
- *Make a list of issues for which we have no or insufficient information.*

### 3.3.3 Sources

Once we have a list of what needs our attention, we have to think where we can find the information. Since we always must be able to crosscheck the information, we need a few sources that can relate about the same issue.

Many sources are quite logic: *if you want to find out what the interest rates are for loans to SMEs, you talk to a few banks. If you want to find out what the policy of the Government is, you talk to the relevant departments.* Other names will come up during the interview as well: the major suppliers of the SMEs, the name of an NGO that provided credits to the SMEs, the school where most SMEs were trained.

You should also pay attention to locating key informants who have a so called helicopter view of the sub sector: people who can give you an overall picture of how the sector works: what are the main trends, the constraints, the opportunities, the major players. You might think of journalists, general economists, retired business men or researchers.

- *Make a list of all potential informants per "block"*
- *Chose three informants per block that seem most ideal:*
  - *Able to provide information about most blocks*
  - *Easy to access*
  - *High level of expertise*
- *Make a list of questions for each informant*

For some blocks it might be difficult to come up with sufficient names. Don't worry: they will come when interviewing the first key informants. When interviewing other key informants, simply ask them if they can think of other key persons that have key information about certain blocks. If you include such questions in your interview you will most certainly come up with other names that will provide you with the missing information. Remember: the objective is to obtain information, not the number of interviews!

#### Who to talk to?

In many cases you will have come up with names of institutions; a government department, the bank or an NGO and the question is who to interview within that institution. The best and easiest way is to simply contact them (phone, visit, avoid official letters, they often take too much time) and inform them about your study. Tell them what the issues are and the sort of questions you have, and ask them who would be the best person to talk to. There are two risks.

1. You will talk to (too) high placed officials who don't know 'reality' or insufficient details and who keep a political speech.
2. You will talk to (too) low placed officials who are not informed about policies or who are 'not authorised' to speak.

In both cases you shall have to use your diplomacy and you will have to make a second appointment with the more appropriate person within that institution. In many cases you will not be able to bypass the 'highest in place' and you shall have to go through procedures. However, these always take time and making use of your network can be very time saving!

### **Prepare your interview**

There is no need to make and test a questionnaire. The type of persons and the type of questions are different and you would waste your time on making various questionnaires. Simply structure the list of questions in such a way (topic wise) that through that 'checklist of issues to ask' you will have a discussion, a dialogue, and not a cross examination with the person!

### **Documents**

Try to find information about the institution: what is their vision, what are their plans, who are their staff? Are there any documents available? The more you know about them before the interview, the better you can formulate your questions. Spending one hour preparing the interview can make the difference between a successful and a not so successful interview: receiving answers to your questions or listening to a waterfall of words that do not have your interests.

Since we are talking with key informants and institutions, they will most likely have much more "on paper". Ask for these documents if you think they are relevant: *do the banks have brochures on loan conditions? Does the government department have a report about last years result? Does the NGO have a plan for the coming three years?*

### **When have we done enough interviews?**

When ever you have the information you wanted! That information needs to be reliable, which means that at least two sources have confirmed the facts and that there are no contradictions in the various replies. Playing the devils advocate will also be useful to check whether you have sufficient and reliable information.

### 3.3.4 The interviews with the suppliers

We have to understand the ins and outs of the supply channels for our SMEs. The availability of supplies is crucial for the performance of the SMEs and we should thus hold interviews with suppliers or even suppliers-of-suppliers. During the interviews with the SMEs we will have heard of many channels and many names of suppliers. The database will provide a listing of names and the map will show us which channels exist.

The number of interviews again depend on the information we obtain. We should at least interview the main actors in *all* supply channels although the number of interviews will be less then the number of SMEs we have interviewed.

In principle we could use the same questionnaire that we have used for our SME interviews, but then we use it from the point of view of the supplier:

- his products
- his markets, his clients
- his suppliers
- his competitors
- his labour force
- his machinery
- the financial aspects

Most likely we will have to adjust the questionnaire slightly: it needs to be less broad and more focussed towards our sub sector. We want to learn about the role these suppliers play for our SMEs: what are their main problems, what are the trends, what is the volume of trade in the sub sector, etc. We also include some crosschecking of the information supplied by the SMEs so that we can also confirm procurement channels.

Of course we also have to create a separate database to process these replies!

*John, Peter and Paul each stated they bought ten cubic meters monthly from TimCom, but TimCom states it has a turnover of 15 cubic meters per month of which it sells half to a large construction company. Do John, Peter and Paul buy their timber elsewhere? Does TimCom cuts more timber than it says it does or holds a license for?*

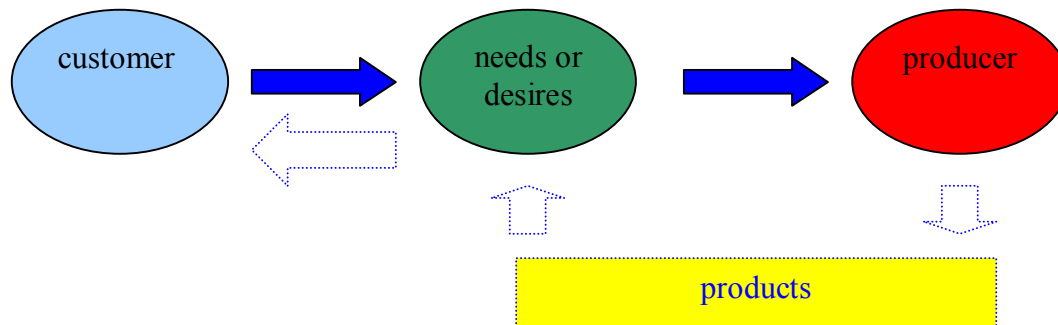
When choosing the suppliers we in first instance focus on the basic raw material: timber cutting for furniture makers and seeds for farmers. However, if certain other inputs appear to be cumbersome (a possible result of the interviews with the SMEs) we might have to include other input suppliers: varnish for furniture makers or fertilizer for farmers.

If possible and needed, we might also want to interview the supplier of the supplier. If the suppliers-of-suppliers have serious constraints, that will influence the suppliers, which in its turn influences the SME: the domino effect.

- *Design the questionnaire for suppliers*
- *Design the database to process these questionnaires*

### 3.3.5 The interviews with the customers

Remember this schedule from the second module?



Customers are an important source of information: we should be checking whether the producers satisfy their needs: are the customers satisfied about the products by the SMEs? We should measure customer satisfaction and that we best do by interviewing a sample of customers and end-users.

The selection of interviewees is crucial. We will most likely be dealing with intermediaries and with end-consumers, either buying directly from the SMEs or from the intermediaries. The map will however give us some direction as to how many channels and which type of customers there are likely to exist. We might also have an idea about the various types of customers there are as a result of the interviews with the SMEs.

We should thus be in a position to define some (segmentation) criteria that will distinguish between the various customers groups (intermediaries, customers, end-users) whereby we should not forget that institutions are a special segment in the market. Depending on the importance of the market segment we will spend more or less time (the number of interviews) on certain groups of customers.

*The sample criteria for the sausage sub sector might look like this:*

*8 customers who buy from shops in town  
 8 customers who buy from major producers  
 8 customers who buy from micro local producers  
 3 shops  
 3 restaurants*

The number of interviews is relatively high but the duration very short: we will be asking only a few quick questions and will not hold in-depth interviews with them. The objective of the interview is to get an impression about:

- the market size
- the various segments
- the preferences and trends

The following standard questionnaire might be adapted to meet the criteria for your sub sector.

- *Design/adjust the questionnaire for consumers*







*Who buys where?*

One instrument that might assist us in defining where the consumers of the various segments procure the products, or in other words, *who buys where*, is the following table:

Actors Segments	Producers			street vendors	shops	markets	Importers	
	micro	small	medium				formal	informal
(income)								
Low	xx	xx		xx		xxx		x
Medium	xx	x	xx		xx	xxx		xx
High			xxx			x	xxx	

In the first row are listed all the possible actors (that might be more than listed here) and in the first column the various possible segments are listed. In this case, the income criteria is used and three segments are defined: low, medium and high income groups. Combining the types of actors and these three segments shows who sells to who, and maybe more important, who of the enterprises does not sell to promising segments. It provides you with the linkages between producers and consumers!

*The micro and small producers don't sell their products to the high income group. This group buys from medium enterprises, at the markets and from formal importers..*

### 3.3.6 Database

You will proceed these interviews in the same way you have done the SME interviews: you continue until you have identified sufficient respondents that meet your selection criteria. The easiness with which you find sufficient customers per group will also give you an indication of the size of the group.

After the interviewing, you shall have to design a database for this consumer survey, whereby care should be taken that you do not mix the various respondents and draw overall conclusions for the entire group. You have to differentiate between the various groups: simply adding the consumption of sausages for restaurants and individuals will give you no information; the consumption for the restaurants and the consumption per individual will differ!

The following database can be used for the previous standard questionnaire, but of course needs adaptation to your sub sector and questionnaire as well:

<b>number</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>6</b>	<b>7</b>	<b>8</b>	<b>Total</b>	<b>Average</b>
<b>location</b>	<i>R</i>	<i>PU</i>	<i>U</i>							
<b>sex</b>	<i>M</i>	<i>F</i>								
<b>age</b>	<i>1</i>	<i>2</i>	<i>3</i>							
<b>family size</b>	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>						
<b>income</b>	<i>L</i>	<i>M</i>	<i>H</i>							
<b>product1</b>	<i>Y</i>	<i>N</i>								
<b>product 2</b>	<i>Y</i>	<i>N</i>								
<b>product 3</b>	<i>Y</i>	<i>N</i>								
<b>volume/time</b>	<i>1</i>	<i>2</i>	<i>3</i>							
<b>frequency</b>	<i>d</i>	<i>w</i>	<i>m</i>							
<b>outlet</b>	<i>ss</i>	<i>nm</i>	<i>ts</i>	<i>tm</i>	<i>p</i>					
<b>reason</b>	<i>ch</i>	<i>qu</i>	<i>re</i>	<i>na</i>	<i>pc</i>	<i>other</i>				
<b>relationship</b>	<i>s</i>	<i>o</i>								
<b>timing / cause</b>	<i>re</i>	<i>sp</i>	<i>re</i>	<i>other</i>						
<b>satisfaction 1</b>	<i>Y</i>	<i>N</i>								
<b>satisfaction 2</b>	<i>vs</i>	<i>s</i>	<i>ns</i>	<i>vu</i>						
<b>price</b>	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>						

A simple overview of the respondents is sufficient: the same set up can be used as with the SME database by coding the replies. However, if you would make separate sheets for each group of respondents per outlet for example, you would easily see possible patterns between the various segments: for example customers from shops are high income customers. It is important that you 'play around' and try to look for these type of indicators and customer profiles.

With these kind of overviews, with a few questions and a few respondents, using averages is not that suitable:

<b>number</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>6</b>	<b>7</b>	<b>8</b>	<b>Total</b>	<b>Average</b>
<b>location</b>	R	R	R	PU	PU	U	U	U		-
<b>sex</b>	M	M	M	F	M	F	F	F		-
<b>age</b>	1	2	3	3	2	1	2	2		2
<b>family size</b>	2	3	4	2	3	2	1	3		3
<b>income</b>	L	L	M	M	L	M	H	H		M

The averages don't tell you that much, the individual information does tell you more:

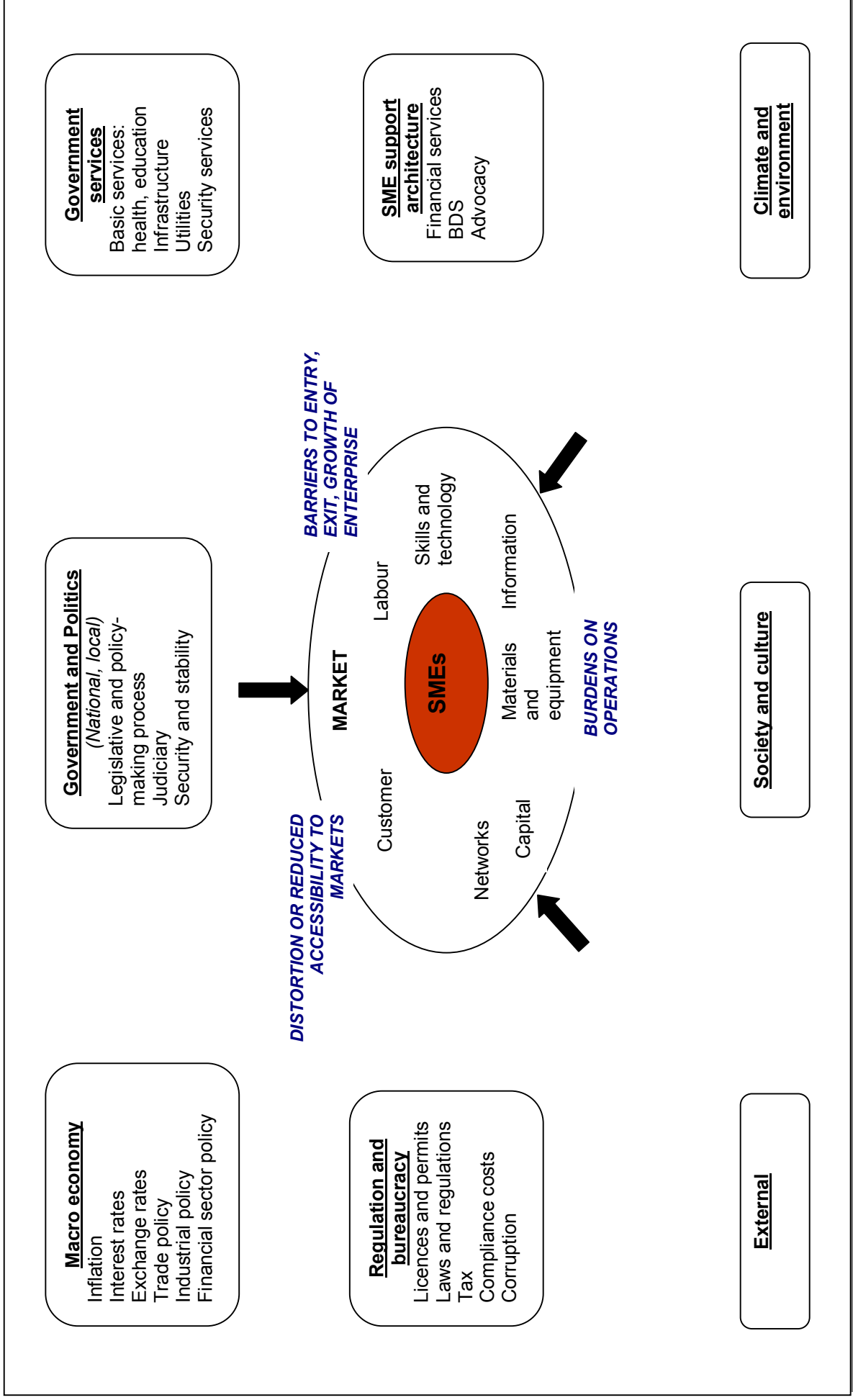
Customers in rural areas have larger families and lower incomes while those who buy from shops appear to be younger, have a higher income and have smaller families. But, most importantly, town shoppers are all female while rural customers are all male! Is this a coincidence or a pattern?

It might indicate that the decision makers (those who buy) are different people (M/F) and that might indicate also that purchasing decisions are different: that you should link to other questions such as the reason for buying the product: one could imagine that town women have other reasons for buying a certain product than rural men: time, quality, price, availability?

This example also shows that 8 respondents for all three groups (rural, peri-urban and urban) is actually insufficient to draw conclusions and that more interviews are required!

- Design/adjust the database for consumers

Figure 1: Main components of the SME environment



## **Tasks Unit 3**

## Tasks Unit 3

### 1 Interviews with key persons

We have prepared the following for the interviews with the key persons:

- A resume of the most crucial information per “block”!
  - A list of issues for which we have no or insufficient information.
  - A list of all the potential key informants per “block”
  - Three informants per “block” that appear ideal
  - A list of questions for each informant
- Prepare your interviews with the key informants
    - Pre-investigations
    - Make appointments
  - Interview!
  - Prepare a small report about the results:
    - What
    - Where
    - Who
    - When
    - Why
    - How

### 2 Interviews with suppliers:

We have prepared the following for the interviews with the suppliers:

- The questionnaire
  - The database.
- Prepare your interviews:
    - Selection criteria for the sample
    - Practical plan for the interviews to be held, including a test-run
  - Interview
  - Process the obtained information in this database

### 3 Interviews with clients:

We have prepared the following for the interviews with the clients:

- The questionnaire
  - The database.
- Prepare your interviews:
    - Selection criteria for the sample
    - Practical plan for the interviews to be held, including a test run
  - Interview
  - Process the obtained information in this database

## **4 Analysis**

## **4.1 Gross Margins**

## 4.1 Gross Margins

### 4.1.1 Introduction

Gross profit is simply defined as *sales minus direct costs* and that gives you an indication of the profitability of the enterprise. To make a true analysis of the profitability by taking into consideration all the *indirect* costs is very complicated. You need very detailed information, which will be difficult to obtain and with the risk of drawing incorrect conclusions if using insufficient or incorrect information.

Gross profit calculations are thus not true profit calculations but they give you a first quick indication: if the gross margin is zero, i.e. the costs are equal to the incomes, you know that the profit will be negative and there is no need to spend much time on defining how negative it will be! However, some caution should be expressed too: if the indirect cost are extremely high, for example if production is with a very expensive machine, the gross margin might be high but the indirect costs (of the machine) might also be very high. In such cases we should, after the gross profit calculation, do a quick profitability calculation.

We will use the gross profit calculation to determine where most profits are being made: in the supply, the production, the wholesale or retail section. That indication might give us some ideas for opportunities and interventions: if the gross profit with the retailers is five times higher than the gross profit of the producers, there is a need to look upstream: that is where 'most money is being made' and there might be opportunities for improving the position of the producers.

### 4.1.2 The information we need

*Gross profit equals the sales minus the direct costs*, and so we need to have information about sales and information about costs. In principle, we have that information from the interviews we have held with the SMEs. We know the selling prices of (most of ) the products that the SMEs produce and we know how many products they sell per week or per production period, so that is not that complicated. The direct cost are more difficult to define.

#### Direct costs

The direct costs are those costs that can be directly attributed to a product: *material and labour costs*.

*The cost of seeds for farmers and the timber for a carpenter, the time a farmer spends weeding and the time a carpenter spends on sandpapering are examples of direct costs.*

The cost of a plough and the electricity for a carpentry workshop, the time the farmer spends with the farmers association and the depreciation of his machinery are examples of indirect costs.

The easiest way to define whether a cost is direct or indirect, is to ask yourself:

*if I produce nothing, do I still face these costs?  
if I double my production, are the costs double too?*

An affirmative answer for the first question implies the cost is indirect.  
An affirmative reply to the second question indicates that it is a direct cost.



- Look at the following expenditures for one month for this carpentry workshop and define which of the costs are direct or indirect:

	<b>direct</b>	<b>indirect</b>
A new drilling machine		
A box of 200 screws		
Telephone bill for June		
License		
Transport for timber bought		
5 litres of glue		
labourer 5 days		
cleaner 20 days		
labourers 3 x 20 days		
materials for repairing the roof		
petrol for the car		
25 planks		
industrial planing of planks		

Whether we take direct labour cost into consideration depends a bit on the accurateness of the information and the sub sector. In principle it doesn't matter if we do or not, as long as we do it consequently and we keep realising whether or not it is included! *If we have included it in the gross profit, we should not do it again in the profitability calculation. But if we don't, we should add these cost when calculating the profitability!*

It is pretty difficult to estimate the cost (time) of direct labour: if a farmer hires labourers during the harvesting season these costs are easy to calculate, but what are the costs (time) a carpenter spends on direct production and how much time does he devote to general issues? If we specifically ask how much time is spend on producing one item, we often get a over- or under-estimation of time. In such case, it best to neglect the direct labour costs in the gross profit calculation.

#### 4.1.3 From gross profit to gross margins

To ensure that we keep realising that we are using simplified gross profit calculations, we will from now on refer to these calculations as Simplified Gross Profit or SGP. Once we have calculated these SGPs, we express them in percentages which we will call Simplified Gross Margins or SGMs, because it will be easier to compare results if we talk about percentages and not about dollars or local currencies.

We calculate the Simplified Gross Profit as follows:

$$\text{SGP} = \text{Selling Price} - \text{Direct Costs}$$

We then calculate the Simplified Gross Profit as follows:

We express everything in percentages by putting the selling price at 100%, i.e. the direct costs and the SGP are a percentage of the selling price:

$$\text{SGM} = \text{SGP} / \text{Selling price} \times 100\%$$

#### 4.1.4 Interpreting SGMs

Look at the comparison between three products: at a first glimpse you might feel that product two is not that interesting since the SGP is lowest.

Product	Direct Costs (1)	Selling price (2)	SGP (3=2-1)	
One	50	75	25	
Two	25	40	15	
Three	75	100	25	
Averages	-	-	-	

Yet, when you calculate the SGM, product two is most interesting: for every dollar you put in that product, you get an additional 37% back in the form of 'margin':

Product	Direct Costs (1)	Selling price (2)	SGP (3=2-1)	SGM (4=3/2x100)	
One	50	75	25	33	(a)
Two	25	40	15	37	(b)
Three	75	100	25	25	(c)
Averages	-	-	-	32	((a+b+c)/3)

It is thus best to draw conclusions from SGMs and not from SGPs. For our study we need to get an impression about the profitability of the SMEs and we can do that by looking at a sample of their usual production. We calculate the SGM for a limited but representative selection of their products as demonstrated in the previous table. That average (32%) tells us that the SGM for that SME stands at 32%; no more, no less. It doesn't say anything about his income or his turnover: in fact; the SGM doesn't have anything to do with the production volume as such (think: we are only talking about direct costs!)

#### 4.1.5 Simplified gross margins in the chain

Let us look at the production of one type of sausages in the chain:

Supplier of raw materials: the butcher  
 Producer: sausage maker  
 Retailer: small shops

*The butcher* buys pigs for \$25 that each result in 25 kg of meat, which he sells for \$2:

Product	Direct Costs (1)	Selling price (2)	SGP (3=2-1)	SGM (4=3/2x100)
Sausage	1	2	1	50%

*The sausage maker* makes half a kg of sausage from one kg of meat, which he sells for \$3: labour cost is excluded and all other inputs (salt, pepper, etc.) are minimal and neglected too.

Product	Direct Costs (1)	Selling price (2)	SGP (3=2-1)	SGM (4=3/2x100)
Sausage	2	3	1	33%

The shop owner sells the sausages for \$5 :

Product	Direct Costs (1)	Selling price (2)	SGP (3=2-1)	SGM (4=3/2x100)
Sausage	3	5	2	40%

Looking at the SGM in the chain we see:

- the butcher            50%
- the producer        33%
- the shop                40%

SGMs are highest with the butcher, then the shop owner and lowest with the producer. Our conclusion might be that profits are also highest with the butcher and lowest for the producer. However, that conclusion is premature.

What are the indirect costs? At this time we cannot draw the conclusion that the producer should slaughter the pigs him self or should sell the sausages himself. Yet, it might be an interesting thought: what are the additional investments or costs?

We should also look at other aspects such as efficiency and scale: if the sausage maker has to buy the pigs, can he buy pigs for the same price? (whereby price is money plus efforts!). What are the additional costs of selling the sausages to the public? (a fridge, one person selling two sausages a day but being paid the whole day?).

Yet, let us assume that the direct costs are the same; we could simply calculate the costs for the sausage maker:

- if slaughtering pigs too:

Product	Direct Costs (1)	Selling price (2)	SGP (3=2-1)	SGM (4=3/2x100)
Sausage	1	3	2	67%

- if selling sausages to the public too:

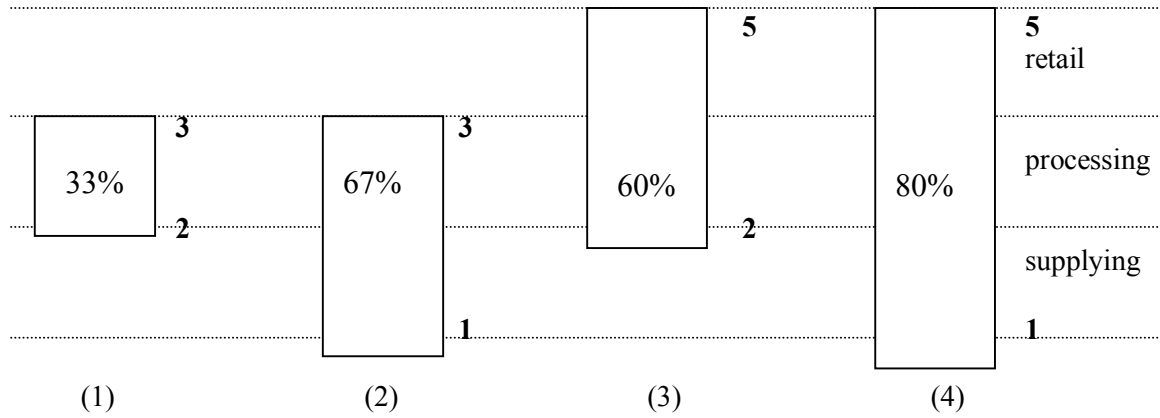
Product	Direct Costs (1)	Selling price (2)	SGP (3=2-1)	SGM (4=3/2x100)
Sausage	2	5	3	60%

- if slaughtering pigs and selling sausages to the public too:

Product	Direct Costs (1)	Selling price (2)	SGP (3=2-1)	SGM (4=3/2x100)
Sausage	1	5	4	80%

- What is the maximum SGM at any time in any situation?

We could also present the four situations as follows:



- Situation (1) the sausage maker buys meat and sells to the shop: a SGM of 33%
- Situation (2) the sausage maker slaughters pigs and sells to the shop: a SGM of 67%
- Situation (3) the sausage maker buys meat and sells to the public: a SGM of 60%
- Situation (4) the sausage maker slaughters pigs and sells to the public: a SGM of 80%

*By presenting the SGMs in this way, you can see at one glance what the SGMs are for each situation!*

**Case A      Anthony the metalworker**

Anthony produces three main products: burglar bars for windows, iron doors and simple safes. He produces on a monthly basis some 25 burglar bars, 15 doors and 5 safes. He buys some 350 iron bars per month for \$1 each, he buys some 90 sheets of iron per year for doors at \$25 each and thick iron sheets for the safes for the total of \$150 per year.

He says he does not hold stocks so the materials bought are used in the same period. He does complain about the safe lock, it'll cost him exactly as much as the cost of sheets per safe! He applies fixed selling prices for each product: \$25 for the average burglar bars, \$50 for doors and \$75 for safes.

- Calculate the average SGM for Anthony's products: first calculate the quantity and cost per product and then calculate the SGM for each product!
  
- why would the direct costs for doors be relatively low compared to burglar bars?
  
- which products seem most attractive to produce?
  
- Calculate the SGM for the workshop, but this time take into consideration the production volume of the three products
  
- How big is the difference in average SGM for the workshop compared to the average SGM for the three individual products? Was that worthwhile the calculation?
  
- Calculate the SGM for the workshop, but this time take into consideration the following production scenario: 50 safes per month and only 5 each of the other products.
  
- How big is the difference in average SGM for the workshop as compared to the average SGM for the three individual products? Was that worthwhile the calculation? What is your conclusion with respect to the SGM and the selection of the product?

#### 4.1.6 Comparing producers through SGMs

We can also use the SGM to compare producers: not all the producers sell for the same price nor do they face the same costs! Let us look at the following comparison of 4 producers producing the same product!

Producer	Direct Costs (1)	Selling price (2)	SGP (3=2-1)	SGM (4=3/2x100)
Producer 1	50	70	20	29%
Producer 2	60	80	20	25%
Producer 3	60	70	10	14%
Producer 4	70	90	20	22%

**Producer 4** sells for a very high price but if we look at the SGM he is only third in rank!

**Producer 2** gets a higher price than **producer 1** but their SGP is the same, while the SGM of producer 1 is even higher! He sells for a lower price but achieves a higher SGM since his direct costs are less!

The influence of the direct costs also shows when comparing **producer 1 and producer 2**: their selling prices are equal, their SGPs are equal but their SGMs differ!

Such kind of analyses can tell us something about the efficiency of the SMEs and show us where constraints and opportunities might be: the production efficiency is often more important than the selling prices!

**Case B Mandy the yoghurt producer**

Mandy has a small yoghurt producing plant. She bought a few machines from the large pre-independence company that was bankrupt and she has been producing yoghurt ever since.

Recently, her nephew for whom she has taken care of all his life, gave her some machines from South Africa and she now has reasonable machinery. Yet, on his last visit to his aunt he noticed that she is not making that much profit. During this leave he wants to analyse how that is possible.

Mandy buys the milk from a few farmers whenever she can. These farmers sell most of their milk to the milk factory at \$1 per 5 litres and to the public (unprocessed) at 50 cents per litre. Maggy pays on average 40 cents per litre. Sometimes the factory can't buy all the milk from the farmers and then Mandy gets it at 20 cents, but often she has to pay the consumer price of 50 cents when there is a shortage of milk.

Mandy doesn't have much direct costs, she processes everything herself without any assistance. She is busy night and day and did think of hiring a hand, but that would cost her another \$10 a week, which she thinks is too much. Her nephew told her to save some \$40 per month to be able to maintain the machinery and replace them after some time.

Her nephew calculated all her other costs and he is surprised to see that these are minimal. Her packing costs, some plastics bags, are 5 cents per litre. She has to use 'starters' to add to the milk to start the process, which costs her \$10 and she has to use it every 100 litres.

She sells most of the yoghurt to boys in the neighbourhood who in turn sell it to the public. She sells at 65 cents to the boys who sell it for 75 cents to the public. Some customers do buy directly from her and then she asks 70 cents.

She sometimes sells yoghurt to one shop who pays her only 60 cents and who sells it for 80 cents a litre. They say they can't pay more because they sell the yoghurt from the milk company at 80 cents too. They only buy her yoghurt because a few customers prefer her yoghurt since it is fresh and with a better taste, but you can't store it as long as the factory yoghurt.

When she argues that the imported yoghurt is triple the price (it is sold for 80 cents too but in these fancy things that only have 33 centilitres) they say it is of a high quality since it is imported and in various tastes like strawberry and other funny additions.

The nephew doesn't know that much about cows (he's a city boy by now) but he read in some article that it can be quiet a profitable business: one cow costs you some \$15 per month on direct costs and they produce some 10 litres a day. He really wants to find out who makes what profit and how his aunt can improve her returns.

His aunt tells him how much sales she had last year:

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<i>Month</i>	<b>lowest</b>	<b>medium</b>	<b>highest</b>
January	300		
February	300		
March	300		
April		500	
May			700
June			700
July		500	
August		500	
September	300		
October		500	
November		500	
December	300		

- Calculate the direct costs for the three situations
- Calculate the SGMs for Mandy for each scenario (3x3=9!)
- Calculate the SGM for the farmers
- Calculate the SGM for both the shop and the street vendors
- Calculate the SGP for Mandy for last year
- Make a map of the chain
- Put the SGMs next to the channels (based upon the purchase price of milk of 40 cents)
- Where are opportunities for Mandy to improve her SGMs?
- The SGMs seem high: what should not be forgotten?



#### 4.1.7 Interpreting sub sector results

The information we obtain through such a SGM exercise does not only gives us indications about the profitability of the sub sector, the constraints and the opportunities. It will also give us information about the size of the sub sector, how many people are employed in the sub sector and how much money is being generated through these activities. The following example might demonstrate how valuable a SGM analysis can be!

##### Case C

Another team who did a similar study in another province with another sub sector provides you with the following results:

	direct costs	selling prices	GPS	GPM
Suppliers	10	20	10	50
Producers	25	35	10	28
Wholesalers	35	50	15	30
Retailers	50	70	20	28

There are 25 producers that on average produce 10 products per month. For one product they need 10 inputs supplied by their suppliers. There are two wholesales and 15 retail shops to whom they sell half their production!

- Why is there a difference between the selling price of the supplier and the purchase price of the producer and is there no such difference between the selling price of the producer and the purchase price of the wholesaler?
- How much inputs supply the suppliers to the 25 producers per month?
- If the average supplier produces 50 inputs per month, how many suppliers do exist?
- How many products do the shops sell?
- If the producers say that one employee produces 1 product in 8 days and the suppliers say that one employee produces 5 inputs per week, how many employees are being employed in the sub sector (excluding outlets)?
- How much money is being generated per month through this sub sector?

## **4.2 Profit Calculations**

## 4.2 Profit calculations

### 4.2.1 Introduction

In the previous section we applied the SGM to SMEs and to the sub sector, but it was also mentioned that in some cases the SGM may need a little bit more consideration. A positive SGP might still result in a negative profit as a result of the indirect costs. This section explains how to make a profit and loss calculation.

### 4.2.2 Structure

A profit calculation takes into account all the costs of the enterprise. For the SGP calculation we included all the direct material and sometimes the direct labour costs, but of course there are many other costs.

- *Can you make a list of all the possible costs that a small producer might face besides the direct material and labour costs?*

It will make things much easier if we order the various cost in the following structure:

<b>Sales</b>		<b>1000</b>
Direct material costs	500	
Direct Labour costs	100	
Total direct costs	600	
<b>Gross profit</b>		<b>400</b>
Indirect Labour costs	80	
Indirect material costs	40	
Other indirect costs	20	
Total indirect costs	140	
<b>Gross before depreciation</b>		<b>260</b>
Depreciation	10	
<b>Profit before tax</b>		<b>250</b>
Taxation	125	
<b>Profit after tax</b>		<b>125</b>

You see that the gross profit in this structure is equal to the SGP: the sales minus the direct costs. However, *sometimes we did not include the direct labour costs in the SGP calculation and for those cases we make a small adjustment to the structure:*

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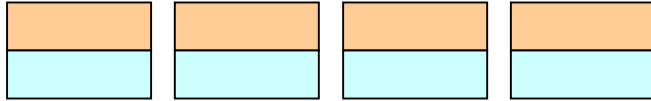
<b>Sales</b>		<b>1000</b>
Direct material costs	500	
<b>Simplified Gross Profit</b>		<b>500</b>
<i>Direct Labour costs</i>	<i>100</i>	
<b>Gross profit</b>		<b>400</b>
Indirect Labour costs	80	
Indirect material costs	40	
Other indirect costs	20	
Total indirect costs	140	
<b>Gross before depreciation</b>		<b>260</b>
Depreciation	10	
<b>Net Profit before tax</b>		<b>250</b>
Taxation	125	
<b>Profit after tax</b>		<b>125</b>

We take the direct labour costs out of the gross profit and what remains is the SGP! Thereafter we include the direct labour costs and what remains is again the gross profit. In this way we can use the already calculated SGP, and simply continue with calculating the profits as per schedule.

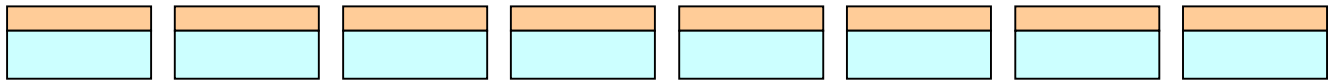
<b>Simplified Gross profit</b>		<b>500</b>
<i>Direct Labour costs</i>	<i>100</i>	
<b>Gross profit</b>		<b>400</b>
Indirect Labour costs	80	
Indirect material costs	40	
Other indirect costs	20	
Total indirect costs	140	
<b>Gross before depreciation</b>		<b>260</b>
Depreciation	10	
<b>Net Profit before tax</b>		<b>250</b>

➤ *Why is it so important to distinguish between direct costs and indirect costs?*

The direct costs are related to the production volume, while the indirect costs are not! So no matter how much we produce, we will still face these indirect costs: they do not change (that much) with a lower or a higher production volume. However, this also implies opportunities: if the total costs don't change and we produce more; than these overall indirect costs can be spread over more products, and thus are the *costs per unit* less!



The indirect (red) costs are spread among a few (4) products



The indirect (red) costs are spread among more (8) products

Let us look at the costs per unit for the given example: the cost were based upon a production of 100 units. By dividing each cost by 100 we get *the costs per unit* (the last 3 columns):

<b>Sales</b>	<b>For all:</b>	<b>1000</b>	<b>For each unit:</b>	<b>10</b>
Direct material costs	500		5	
Simplified Gross profit	500		5	
Direct Labour costs	100		1	
<b>Gross Profit</b>	<b>400</b>		<b>4</b>	
Indirect Labour costs	80		0.8	
Indirect material costs	40		0.4	
Other indirect costs	20		0.2	
Total indirect costs	140		1.4	
<i>Gross before depreciation</i>	<i>260</i>		<i>2.6</i>	
Depreciation	10		0.1	
<i>Net Profit before tax</i>	<i>250</i>		<i>2.5</i>	

The gross profit for each unit is \$4 (10-5-1) but the net result is only \$2,5 due to the other indirect costs (0,8 + 0,4 + 0,2 + 0,1).

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Now if we would produce *200 units* during the same period, the result would be as follows:

<b>Sales</b>	<b>200x10</b>	<b>2000</b>
Direct material costs	200x5	1000
<b>Simplified Gross profit</b>		<b>1000</b>
Direct Labour costs	<b>200x1</b>	<b>200</b>
<b>Gross Profit</b>		<b>800</b>
Indirect Labour costs		80
Indirect material costs		40
Other indirect costs		20
<b>Total indirect costs</b>		<b>140</b>
<b>Gross before depreciation</b>		<b>660</b>
Depreciation		10
<b>Net Profit before tax</b>		<b>650</b>

The income doubles from 100 units x \$10 to 200 units x \$10.

The direct costs *per unit* remain that the same, but the number of units change from 100 to 200: direct material from 100 units x \$5 becomes 200 x \$5 and the direct labour costs from 100 units x \$1 becomes 200 units x \$1. In other words: the direct costs and the gross profit double too!

The indirect costs do not change at all and remain at \$140.

The net result is thus much higher (\$650 compared to \$250) because the indirect costs are now spread among 200 units ( $140/200 = \$0,7$  per unit) compared to \$1,4 per unit ( $140/100$ ).

The above examples show us that:

- The SGP depends on the selling price
- The SGP depends on the direct costs
  
- The net profit depends on the size of the indirect costs
- The net profit depends on the number of units produced

CAPSA

Let us again look at the business of *Anthony, the metal worker* who produced burglar bars, doors and safes and whose information resulted in the following table:

Product	Direct Costs (1)	Selling price (2)	SGP (3=2-1)	SGM (4=3/2x100)
Burglar bars	14	25	11	44%
Doors	12.5	50	37.5	75%
Safes	5	75	67.5	90%
Averages				<b>70%</b>

Now that we know that indirect costs are important too, we discuss with Anthony what his indirect costs are and he informs us that his indirect costs are \$20.700, specified as follows:

Indirect materials	4.000	
Labourers	6.000	
Telephone	0.600	
Insurance	0.600	
License	0.500	
Electricity	4.800	
Maintenance	1.000	
Rent	1.200	
Total other indirect costs	8.700	
Depreciation	2.000	
<b>Total</b>		<b>20.700</b>

The indirect material costs (\$4000) as well as the labour costs (\$6000) we had not included in the direct costs because it was too complicated, too much guessing about what was used for which product and that is why we included it under the indirect costs. The depreciation ( the amount that Anthony should set aside to replace his machines one day) is put at \$2000. From Anthony's sales records we know that the total sales were some \$30.000.

We can now make a profit calculation using the information from the SGP: the average SGP was 70% and that implies that the direct material costs were 100-70=30% of the sales!

<b>Sales</b>		<b>30.000</b>	<b>100%</b>
Direct material costs	09.000		30%
<b>SGP</b>		<b>21.000</b>	<b>70%</b>
Direct Labour costs	0		
<b>Gross profit</b>		<b>21.000</b>	
Indirect labour costs	06.000		
Indirect material costs	04.000		
Other indirect costs	08.700		
Total indirect costs	18.700		
<b>Gross before depreciation</b>		<b>02.300</b>	
Depreciation	02.000		
<b>Net Profit before tax</b>		<b>00.300</b>	<b>01%</b>

- *Why is the difference between Anthony's SGP and Net Profit so huge?*
- *What advice can you give to Anthony?*

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When calculating the SGP we excluded the welding rods, but now we see that their cost are very high and so it would be best to include them in the SGP. That implies that he should keep a record of how many welding rods he uses for each type of product. It does not mean that his net profit will improve, but it will give him insight as to which product consumes more welding rods and that will give him information for the selling prices or where he should try to make savings!

Suppose Anthony listens to our advice and he analyses his production. He then tells us that from the \$6000 on labour costs, some \$5000 are direct costs for the three products and that from the \$4000, some \$3000 were spend on the welding rods. We could then make the following profit calculation:

<b>Sales</b>		<b>30.000</b>	<b>100%</b>
Direct material costs	12.000		<i>(9000+3000)</i>
<b>SGP</b>		<b>18.000</b>	<b>60%</b>
Direct Labour costs	05.000		
<b>Gross profit</b>		<b>13.000</b>	<b>43%</b>
Indirect Labour costs	01.000		<i>5000 were direct costs</i>
Indirect material costs	01.000		<i>3000 were direct costs</i>
Other indirect costs	08.700		
Total indirect costs	10.700		
<b>Gross before depreciation</b>		<b>02.300</b>	
Depreciation	02.000		
<b>Net Profit before tax</b>		<b>00.300</b>	<b>01%</b>

We see that the calculation is different but that the net result is the same! However, with this information we can analyse the production and see what changes might be required. Let us assume what would happen with the net result if Antonio would double his production:

<b>Sales</b>		<b>60.000</b>	<b>100%</b>
Direct material costs	24.000		
<b>SGP</b>		<b>36.000</b>	<b>60%</b>
Direct Labour costs	10.000		
<b>Gross profit</b>		<b>26.000</b>	<b>43%</b>
Indirect Labour costs	01.000		
Indirect material costs	01.000		
Other indirect costs	08.700		
Total indirect costs	10.700		
<b>Gross before depreciation</b>		<b>15.300</b>	
Depreciation	2000		
<b>Net Profit before tax</b>		<b>13.300</b>	<b>22%</b>

His net result would improve from 1% to 22%. But is it realistic to assume that he can double his production so easily? Producing is one, selling is another! So maybe Anthony should try to look for cost savings? What would happen with the net result if he could save some \$1000 on the rods and another \$1000 on the direct labour?



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<b>Sales</b>		<b>30.000</b>	<b>100%</b>
Direct material costs	11.000		-1000
SGP		19.000	63%
Direct Labour costs	04.000		-1000
<b>Gross profit</b>		<b>15.000</b>	<b>50%</b>
Indirect Labour costs	01.000		
Indirect material costs	01.000		
Other indirect costs	08.700		
Total indirect costs	10.700		
<b>Gross before depreciation</b>		<b>04.300</b>	
Depreciation	02.000		
<b>Net Profit before tax</b>		<b>02.300</b>	<b>08%</b>

His net result would improve from 1% to 8%, which might not look so impressive, but is still eight times more than before!

### 4.2.3 Depreciation

We have been using depreciation in our profit calculations. Let us have a closer look. Depreciation has many definitions but in principle it is not much more than the amount of money we should save in order to replace the machines one day. Some machines only last a few years, others will last 25 years or more. But one day that day will come and we will need money to buy new machines. Despite the many rules and methods for calculating the amount, we only have to ask ourselves two questions:

- *how long will we be able to use the machine?*
- *how much does it cost to replace the machine today?*

A machine lasts 10 years and it costs \$20.000 today. That implies we set aside each year  $20.000/10$  years = \$2000. After ten years we can buy a new machine: (10 years x 2000 = 20.000)

Unfortunately it is not always that simple. Machines tend to get more expensive every year and we don't know how much it will cost in 10 years from now. More troublesome, many SMEs use machinery from pre-colonial days and we don't know the price, and if we do, that price is no longer relevant.

Suppose that one enterprise uses a machine that 25 years ago did cost \$10.000 and would last 50 years, then the depreciation would have been \$200 per year. Even if they would have saved that \$200 every year (which they probably haven't!) it would never be enough to buy that same machine because it might cost as much as \$50.000 today! So that means that we don't ask or use historical prices, but we have to find out what the price of equivalent machines is today!

It will often result in huge amounts for machinery and a good analysis (costs, life span) is thus important. However, most existing SMEs have never used such calculations and have never build up capital to replace their machines: that is why we say that many enterprises are de-capitalised: there is not enough gross profit to replace, or the profits have been 'eaten'.

## Concluding

Making proper profit calculations is complicated! We should therefore be aware of our limitations: most of the time it will be difficult to obtain all the necessary information. In such cases it would be better *not* to apply a profit calculation than to use a profit calculation that is based upon *wrong* information!

Moreover, making a profit calculation is no more than describing the production in a financial language and that is not our task at this stage! The structure for the profit calculations does give us some information about the performance of the enterprise and a first indication of the costs structure, and thus about the constraints and opportunities. We should thus not try to attempt to make a 'perfect profit calculation' but to question each component and see what are the causes and the relations, and what can be improved!

## **4.3 SWOT Analysis**

### 4.3 SWOT analysis

#### 4.3.1 Introduction

A handy instrument to assist you in making an analysis is the so called SWOT analysis. One of the results of your interviews is a list of positive and negative aspects (the aspects you noted on your last sheet of the questionnaires for the interviews). The SWOT will help you in handling these aspects in order to come to an analysis. In fact, such a SWOT can be used for 'any issue' as demonstrated in the following example!

#### 4.3.2 Josef the economist

Josef is an economist in a provincial capital in Angola. He has completed a masters degree but he has no experience yet and is still very young. There are only a few jobs for economist in this town, at least not the type of jobs that were promised to him when he started studying and that are usually desired by economists. In fact, these jobs are getting less everyday. In the old times with central planning, the government departments were big and most economists would be offered a job with the government. Now it seems that only NGOs employ economists, but they only want to employ them if they have experience. Josef has noted that a lot of experienced economists that were previously working in Portugal are now returning to Angola.

While studying he was told that, and he agrees, he is not so good at macro economics. Frankly speaking, he doesn't like that at all! He was best at the more business type of economics; he was good at business administration and commercial management. He has a lot of fun in managing the football club, whereby he is praised for his skills to manage people. He can really motivate the youngsters and he is also good in talking to business owners and government officials in making funds available for the club. In fact, some people refer to him as a fast talker, but then in a positive way;

When Josef talks to these business owners, a lot of them complain about the changes in the system. The former big shop owners, especially the rural based traders, complain that things are changing and that they can't understand it anymore: their business is going down. On the other hand, Josef sees a lot of new companies from abroad who seem to have a lot of money to spend and that are setting up enterprises in this town. They have a problem in finding qualified personnel, especially bookkeepers and managers. Some of them bring their staff from Luanda or even from further!

Josef one day sits down on the veranda to reconsider his position. He lists down all the positive and negative aspects for *his* situation as follows:

#### Positive aspects

He is a qualified economist  
 NGOs are looking for economist with experience  
 He is good at managing people  
 The business owners don't understand the changes in the economy (and realise that!)  
 There are new business coming in from abroad  
 He is a fast talker  
 He is experienced in fund raising  
 He has experience with football club management  
 These new companies have a lot of money  
 These new companies look for personnel  
 Bookkeepers and managers seem difficult to find

#### Negative aspects

He has no experience in 'real jobs'  
 He is still young  
 There are less jobs offered by the government  
 There are more experienced economist  
 There are experienced economist returning  
 He is not good at macro economy

*Josef is somehow pleasantly surprised that there are still so many positive aspects: he just wonders why he is still unemployed!*

### 4.3.3 Controllable or non controllable aspects

The above listing of positive and negative aspects can be specified further. Some aspects are typically for Josef: they are *his* strengths and weaknesses. He himself can do something to change them!

One of his strengths is that he is a qualified economist, he has done a masters degree. If he would do his PhD, he would be more qualified: so he would improve one of his strengths even more.

One of his weaknesses is that he is not so good at macro economics. If he would take extra lessons or another course, he might make that weakness less weak, or turn it even into a strength by getting better at macro economic issues.

Yet, there is nothing he can do about the fact that the government is offering less jobs: he can not influence that policy: he can apply for the few jobs on offer, but he can not make the government to offer more! That is why this is not a weakness of Josef but it is something negative that is out of his control. We therefore call it a threat!

Josef can also not do anything about the fact that new companies are looking for staff, that is a fact, but that fact offers an opportunity for him: it is positive but not controlled by him!

This is the basis for the SWOT analysis; we look at all the (positive and negative) aspects and separate between controllable aspects (strengths and weaknesses) and not-controllable aspects (opportunities and threats). The non-controllable aspects are important even though we can't do something about them directly. We need to realise that these threats and opportunities exist for us to define strategies. Sometimes we also refer to the controllable aspects as *internal* and to the not-controllable aspects as *external*. It is scheduled as follows:

	<b>Positive</b>	<b>Negative</b>
<b>Internal</b>	Strengths	Weaknesses
<b>External</b>	Opportunities	Threats

Josef thus re-organises his lists as follows:

	<b>Positive</b>	<b>Negative</b>
<b>Internal</b>	<p><b>Strengths</b></p> <p>A qualified economist. A fast talker. Experience with football club management. Experienced in fund raising. Good at managing people.</p>	<p><b>Weaknesses</b></p> <p>Not good at macro economy. No experience in 'real jobs'. Still young.</p>
<b>External</b>	<p><b>Opportunities</b></p> <p>NGOs are looking for economist with experience. The business owners don't understand the changes in the economy (and realise that!). There are new business coming in from abroad. These new companies have a lot of money. These new companies look for managers and bookkeepers. That type of staff seems difficult to find.</p>	<p><b>Threats</b></p> <p>Less jobs offered by the government. More experienced economist. Experienced economist returning.</p>

Josef now realises that most of the positive aspects are actually opportunities and not so much his strengths. At first he is not that happy, but then he realises that opportunities are at least as important as his strengths! He also realises that a weakness of others (such as the problem the business owners have) might actually be an opportunity for him!

#### 4.3.4 Case Mandy the yoghurt producer

*Let us have another look at Mandy the yoghurt producer:*

Mandy has a small yoghurt producing plant. She bought a few machines from the large pre-independence company that was bankrupt and she has been producing yoghurt ever since.

Recently, her nephew for whom she has taken care of all his life, gave her some machines from South Africa and she now has reasonable machinery. Yet, on his last visit to his aunt he noticed that she is not making that much profit. During this leave he wants to analyse how that is possible.

Mandy buys the milk from a few farmers whenever she can. These farmers sell most of their milk to the milk factory at \$1 per 5 litres and to the public (unprocessed) at 50 cents per litre. Mandy pays on average 40 cents per litre. Sometimes the factory can't buy all the milk from the farmers and then Mandy gets it at 20 cents, but often she has to pay the consumer price of 50 cents when there is a shortage of milk.

Mandy doesn't have much direct costs, she processes everything herself without any assistance. She is busy night and day and did think of hiring a hand, but that would cost her another \$10 a week, which she thinks is too much. Her nephew told her to save some \$40 per month to be able to maintain the machinery and replace them after some time.

Her nephew calculated all her other costs and he is surprised to see that these are minimal. Her packing costs, some plastics bags, are 5 cents per litre. She has to use 'starters' to add to the milk to start the process, which costs her \$10 and she has to use it every 100 litres.

She sells most of the yoghurt to boys in the neighbourhood who in turn sell it to the public. She sells at 65 cents to the boys who sell it for 75 cents to the public. Some customers do buy directly from her and then she asks 70 cents.

She sometimes sells yoghurt to one shop who pays her only 60 cents and who sells it for 80 cents a litre. They say they can't pay more because they sell the yoghurt from the milk company at 80 cents too. They only buy her yoghurt because a few customers prefer her yoghurt since it is fresh and with a better taste, but you can't store it as long as the factory yoghurt.

When she argues that the imported yoghurt is triple the price (it is sold for 80 cents too but in these fancy things that only have 33 centilitres) they say it is of a high quality since it is imported and in various tastes like strawberry and other funny additions.

The nephew doesn't know that much about cows (he's a city boy by now) but he read in some article that it can be quite a profitable business: one cow costs you some \$15 per month on direct costs and they produce some 10 litres a day. He really wants to find out who makes what profit and how his aunt can improve her returns.

- *Make a SWOT analysis for Magdalena*

#### 4.3.5 SWOT analysis for your sub sector.

Take into consideration your findings from interviewing the SMEs, the suppliers, the customers and the other interviews and other sources of information such as documents.

- Make an overview of these positive and negative aspects using the SWOT schedule: strengths, weaknesses, opportunities and threats.

### 4.3.6 Winning combinations and major challenges

Identifying the controllable and non-controllable aspects gives us some information, but the next step will help us even more! We will now confront the strengths with the opportunities and the weaknesses with the threats.

We then first look at the combination of strengths and opportunities and decide which of those is most relevant:

<p><b>Strengths</b></p> <ol style="list-style-type: none"> <li>1 a qualified economist</li> <li>2 a fast talker</li> <li>3 experience with football club management</li> <li>4 experienced in fund raising</li> <li>5 good at managing people</li> </ol>
<p><b>Opportunities</b></p> <ol style="list-style-type: none"> <li>1 NGOs are looking for economist with experience</li> <li>2 The business owners don't understand the changes in the economy</li> <li>3 There are new business coming in from abroad</li> <li>4 These new companies have a lot of money</li> <li>5 These new companies look for managers and bookkeepers</li> <li>6 That type of staff seems difficult to find</li> </ol>

If we confront the first strength (qualified economist) with the first opportunity (NGOs looking for experienced economists) we see that the combination of these two is not very relevant: NGOs look for experienced economists and not (only) for qualified economists.

- *Confront each strength with each opportunity and decide whether it is relevant: order the combinations and choose the most relevant combination: not the individual strength or opportunity, but the combination of the two will be your winning combination!*

The same we do for the weaknesses and threats; we confront each weakness with each threat and look for the most probable combination; that is then our major risk or in other words: a challenge for us to improve!

<p><b>Weaknesses</b></p> <ul style="list-style-type: none"> <li>not good at macro economy</li> <li>no experience in 'real jobs'</li> <li>still young</li> </ul>
<p><b>Threats</b></p> <ul style="list-style-type: none"> <li>less jobs offered by the government</li> <li>more experienced economist</li> <li>experienced economist returning</li> </ul>



Josef makes such confrontations and comes up with the following combinations:

**winning combination:**

he is good in managing people *and* new companies look for managers

**most probable challenge:**

he has no experience in 'real jobs' and experienced economists return

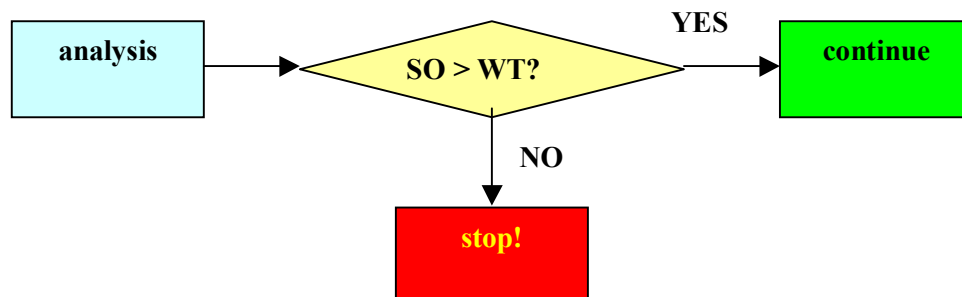
For Josef this means that he should define a strategy whereby he looks for other openings in the employment market (managers), whereby he can make use of his major strength (managing people). Due to his weakness of not having real job experience combined with the danger of returning economist, he might also opt to apply for these positions (when the labour market for economists becomes tighter), which is his major challenge.

One option would be that he looks for additional strengths (local knowledge, resident, networks) that will reinforce his strength for him to be able to compete on the market. His major weakness, no experience, he could improve by for example in first instance look for 'less rewarding' jobs as soon as possible and thereby replacing his weakness of 'no experience' in to 'local experience'. That would turn his weakness into a strength since returning economist will not have that local experience.

- *Could you think of other options?*
- *Define the winning combination and major challenge for Mandy the yoghurt producer.*
- *Define the winning combination and major challenge for your sub sector.*

#### 4.3.7 Go or No-Go?

After the SWOT we ask ourselves whether the Strengths & Opportunities override the Weaknesses & Threats. In other words: is there a winning combination that can overcome the major danger? If the answer is YES, we will continue our research and design interventions that will improve the performance of the sub sector. However, if the answer is NO, we have to accept that there is no future for this sub sector. No intervention will improve that!

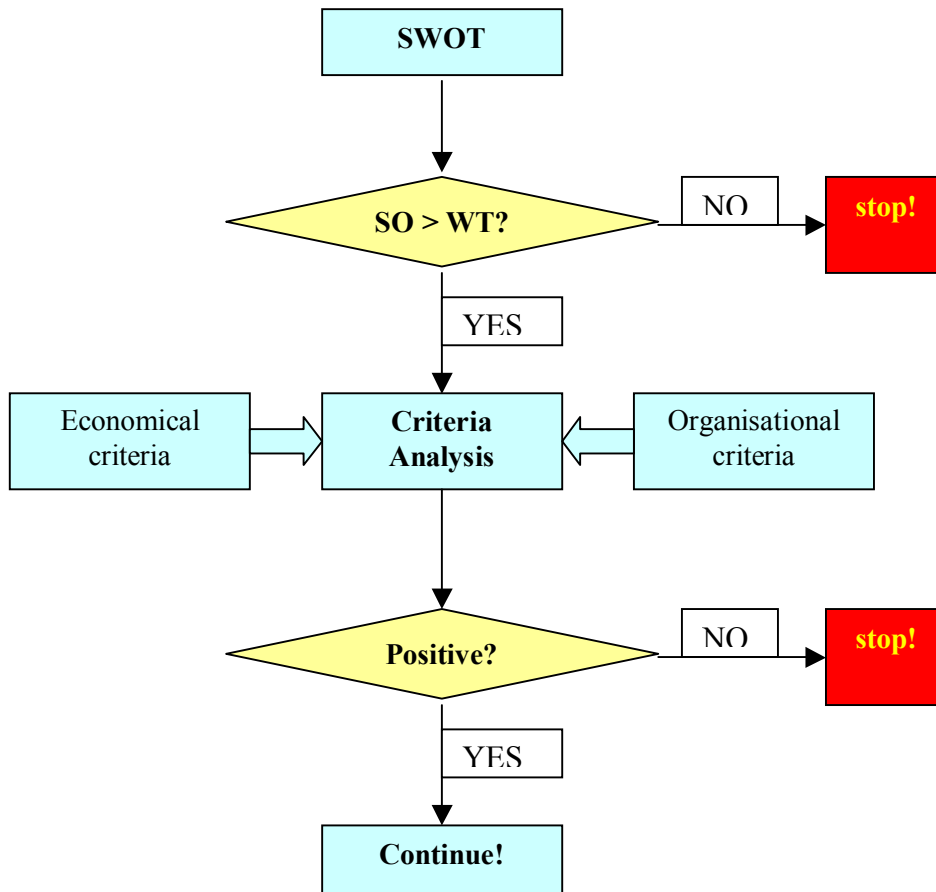


## **4.4 Sector Criteria**

## 4.4 Sector criteria

### 4.4.1 Introduction

We have done the SWOT and we have a positive outcome: the Strengths & Opportunities override the Weaknesses & Threats or in other words: there is a winning combination that can overcome the major danger! We could thus move on to the next phase of identifying and designing interventions. However, there exist a few additional criteria that will assist you in this process of deciding whether interventions the sub sector are worth while. These criteria are based upon economical and organisational considerations. We will start with the economical criteria.



### 4.4.2. Employment creation

Employment will generate income to people and is therefore often a major criterion. Creating employment might be within the SMEs in the sub sector, but might also be elsewhere in the chain! An intervention that improves the functioning of the sub sector might increase production volumes. As a result, more SMEs might start, or existing SMEs might employ more employees. It might also result in more employment with the suppliers or the retailers.

It is difficult but not impossible to estimate how many SMEs and employees are involved in the sub sector: that information might be available from other studies or documents, but you probably can find that also from your interviews with the SMEs. You have certain averages of employees per (group of) SMEs and you can find out how many SMEs exist. The same logic you can apply to the other actors in the chain.

#### 4.4.3 Added chain value

The higher the value that is added in the chain, the more valuable that sub sector is for the region: "money is being created locally". Let us compare locally grown potatoes and imported potatoes:

*In order to grow potatoes locally one has to buy seeds and fertilizer elsewhere and let us assume that these cost \$10 per unit. The grown potatoes are sold at the market at \$100 per unit. The added value equals  $\$100 - \$10 = \$90$  per unit; we have created \$90 and that money stays in the province: it is ours!*

*When buying potatoes from elsewhere, let us assume we pay \$60 per unit and we sell the potatoes at the local market also for \$100 per unit. In this case we have added  $\$100 - \$60 = \$40$  per unit: we have created only \$40 because the \$60 leaves our province again!*

So the higher the added value, the more advantageous this sub sector is for our local economy. In its simplest form we look at the sales value (the last price in the chain) and deduct the first purchase price (the first price paid to the first actor in the chain). This will give us a first indication of the added value and will be sufficient in most cases. In some cases, for example where additional inputs elsewhere in the chain are extremely high, we have to deduct these external inputs.

#### 4.4.4 Volumes

We should have an indication about the volumes that are manufactured and traded in the sub sector in order to determine how important the production of this sub sector is for the local economy. Besides the created employment and added value, the local economy might benefit from this sub sector because the people need the products: a very obvious case is the local production of basic commodities. Even though the employment created is not that significant (for example because the production is not that labour intensive) and with only little added value (because the value of the good is not that high), it might still be important because 99% of the population uses the goods.

#### 4.4.5 Self sustainability

In how far is the chain dependent on other actors, outside the local economy? This is related to the added value principle but then in non-monetary terms: how risky is the relationship with external suppliers? In how far will external factors affect our chain productivity?

*If we buy seeds from a neighbouring country at a very low cost, what will happen if the economy of that country faces an extreme inflation; the costs of the input will go up while our local customers will not be able or willing to pay the higher consumer price.*

Although we most often look at the supply side, we could also look at the market side: if our market is not local (and in such cases the added value is usually high!) what does this mean for our production chain?

*If we sell our products to the capital, that market might be favourable at this moment, but is also at a distance and other suppliers might easily enter that market. What are the alternative outlets in such case?*

#### 4.4.6 Government policies

Although not a criterion as such, it is important that we take into consideration the policy of the government regarding our sub sector. To a certain extent this we will have done during the information gathering phase and the SWOT analysis, but it is recommended to spend some additional time on analysing the consequences.

*It is probably very profitable to stimulate (illegal) diamond delving but it is doubtful that this is in line with the government policy, while it will be difficult to find donors to finance such an intervention.*

*If the government policy is to promote larger scale enterprises and wishes to reduce the so called informal economy by forbidding micro activities and if our sub sector is highly informal, we should analyse the consequences: the government policy becomes our major challenge!*

- *Define your economic criteria*
- *Calculate the values for this sub sector for each criterion*

#### 4.4.7 Organisational criteria

There might be other non-economical criteria that you might apply to your sub sector analysis.

*You are an organisation that supports female entrepreneurship and you might add as a criterion that a certain percentage of the entrepreneurs should be female. Hence, there must be scope in the sub sector for female entrepreneurship*

Other criteria might be related to human dignity, marginalized groups, youth, elderly or the environment. These depend on your organisation and its mission! It is thus important to discuss at the appropriate levels which criteria are most important for your organisation and how these can be operationalised.

- *Define your organisational criteria*
- *Operationalise each criterion for this sub sector*

#### 4.4.8 Go or No Go?

Now that we have defined and calculated the values for each criterion, we can decide whether they meet our standards and expectations. This is best done in a group session, involving the highest organisational levels.

## **Tasks Unit 4**

## **1 Simplified Gross Margins**

- Verify whether you have sufficient information to calculate the SGMs of a representative sample products of some groups of producers.
- If not, select a sample of actors and collect the information through some additional interviews.
- Calculate the SGMs for all the actors in the chain.
- Transfer the SGMs to the databases and the sub sector map.
- Analyse the map.

## **2 Profit and loss calculation**

- Select three representative producers and collect the necessary information to make a complete profit and loss calculation.
- Analyse your findings for the sub sector.

## **3 Present your results to the producers**

- Complete your SWOT analysis and your map (see unit 4.3) with the new information.
- Present your findings and conclusions of the SWOT, the map and the SGMs to a group of producers and discuss your analysis with them.

## **4 Present your results to your directors:**

- Update your SWOT analysis and your map with the new information obtained through the above session.
- Define and calculate the necessary data to apply the economic criteria.
- Present your conclusions and proposals for the sub sector in a meeting with your decision makers.

## **5 Present your results to the actors in your sub sector**

- Prepare a presentation (as above) to a the key actors in your sub sector and discuss your analysis.
- Write a resume with the main conclusions and improve your SWOT and map with the outcome of the above session.

## **5 Principles**



## **5.1 Organisational Landscaping**

## 5.1 Organisational Landscaping

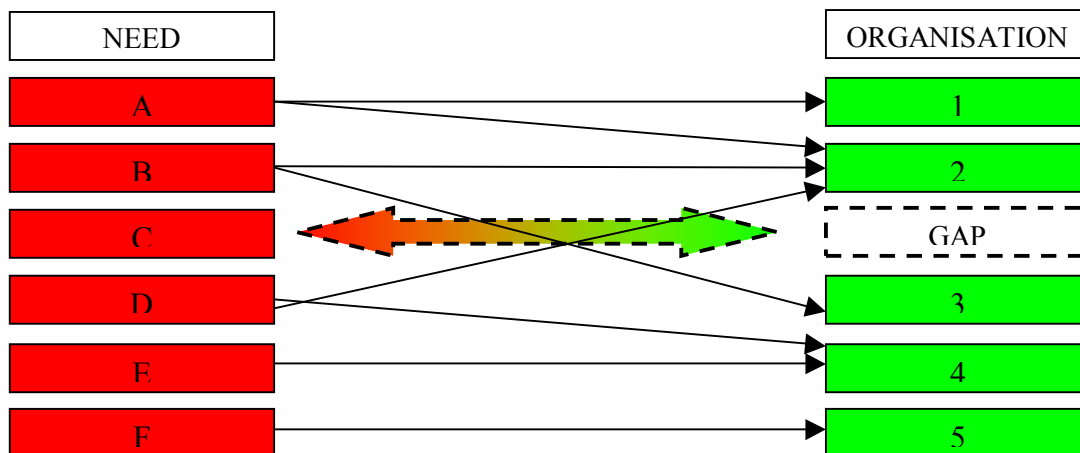
### 5.1.1 Introduction

*In one of the provincial capitals, one NGO wanted to support the SMEs and did a lot of research to identify the main problem of the SMEs. She came to the conclusion that access to credit was the main problem and they designed a credit programme and sought funds from a large donor. The donor agreed, but pointed out that for such a programme to be successful they needed at least 150 loans per year as a critical mass. Since there were 300 enterprises that had indicated such need, the NGO responded that that would be no problem. But soon after launching the programme, the NGO discovered that another NGO had also started a credit programme at an even bigger scale, for which it also needed a critical mass of some 250 loans!*

Organisational landscaping would have prevented such grave errors. Landscaping is no more but also no less than a structured investigation into the presence, activities and plans of organisations (governmental, non governmental, banks, trade organisations and others) that might be relevant for the SMEs in general and for the enterprises in the sub sector in particular.

### 5.1.2 The principle

Knowing the needs of the sub sector and knowing what is being done by who, we can identify the gaps: needs that are not addressed by other organisations



Need A is addressed by organisation 1 and 2 while organisation 2 addresses need B & D too! Needs E and F are taken care of by organisation 4 and 5 respectively, while need D is also addressed by organisation 4, just as need B is addressed by organisation 3 too. It seems that nobody is looking into need C. That is a gap we could fill!

The above schedule reminds us of a SWOT analyses for an enterprise; where are the needs of our clients, what kind of opportunities do we see, and what is the competition NOT doing? That is the way we should look at the exercise: a business oriented approach. Only by such a business approach we will serve our clients best, fulfilling their needs that are not met by other organisations!

### 5.1.3 The approach

While interviewing the SMEs and key persons, some names will have popped up when the right questions were asked: *where do SMEs get loans from, where were they trained, who assisted them making their business plans?*

- *Make a list of organisations that have been mentioned in the interviews.*

Refer to your sub sector map and SWOT analysis and "imagine" what other actors might exist and that are not yet on your list. Who might be involved in technology, who could be training farmers, who should be advocating and which financial services might be available?

- *Make a list of organisations that might or might not be active in one of these fields*

This list is thus different from the previous one: we don't mention organisations of whom we are sure they *are active*, but we make a listing of possible organisations that *might be active*.

Don't limit your search to those that address your sub sector. Include organisations that focus on SMEs in general. Also include organisations that are addressing other sub sectors. These organisations might have a specific approach for that sub sector but that might be interesting for this sub sector as well, or they might even be considering to offer their services to your sub sector too.

Once we have the lists, we make a visiting schedule whereby we start with the most promising organisations: those of whom we are sure they are interesting for our sub sector. At the same time we make telephonic enquiries with those organisations that we are not so sure of whether they are interesting to visit. Depending on that outcome, they are included in our schedule, or not.

We then prepare our interviews in a similar way as we did before: we focus on the most relevant and interesting issues for which we prepare some questions. There is no need to prepare questionnaires: we can make a "checklist of issues and questions" according to the issues we want to discuss with each organisation. Some of the organisations we might have interviewed as key informants and it depends on that outcome whether we need to re-interview them. This time we don't want information about the sub sector but we want information about them! Most of the questions you can structure around the questions: *what, why, who, when, where and how!* Besides these questions about their organisation, you also want to find out with whom they cooperate, what is their relationship: who else is out there doing what! The objective is to get a complete picture of who is doing what!

- *Make a one page checklist for each organisation*

Visit the organisation. Include sufficient time for the introduction and for taking away misconceptions. Some institutions might not be too eager to provide you with information on their functioning. They might simply not be interested in sharing experiences or they might be afraid of "competition" or "criticism". Take away that perception, be open and honest and avoid an 'evaluators attitude'.

Process the information. Make a one page summary of your findings ( *the what why who when where and how questions*) and refer or annex any documents that you might have received.

Besides the summarised information per organisation, we also have to present the overall landscape for which we can use the previous division:

Organisation	Technology		Business Development						Financial Services				Advocacy		Remarks
			training			Advisory Services	Market Linkages	micro/small/medium				Overall policies on SED	Sub / Sector specific		
	Vocational Training	Product Development	Entrepreneurial	Business Management	Farm Management					Micro Finance	Revolving funds			Capital investments	Others ( ..... )
1															
2															
3															
4															
5															

We simply tick the appropriate box and put key words about sub sectors, coverage and other key information in the last column. It should be noted that the above summary is no more than an overview and you are therefore free to adjust and restructure the schedule: if there are more financial instruments, include them. If you want to specify between sub sector and general organisations, do so!

#### An example:

Organisation	Technology		Business Development						Financial Services				Advocacy		Remarks
			training			Advisory Services	Market Linkages	micro/small/medium				Overall policies on SED	Sub / Sector specific		
	Vocational Training	Product Development	Entrepreneurial	Business Management	Farm Management					Micro Finance	Revolving funds			Capital investments	Other (leasing)
1	abc	x		x	x									x	construction
2	def		x			x		x						x	farmers
3	ghi						x	x					x		
4	ijk							x					x		
5	lmn											x			food industry

The above example tells us that there are no organisations that offer loans for capital investments. If the outcome of our sub sector analysis would have been the lack of access to capital for investments, we see that none of the organisations addresses that need. Talking to the 4th organisation about their experience with micro finance (working capital) and discussing their expansion might be a first option. The 5th organisation might also be interesting; they are operating only for the food sector but might be interested in expanding to other sub sectors.

#### 5.1.4 A double confrontation

Confront the needs (the outcome of your SWOT analysis) with the identified organisations. If there appear gaps, ask yourself whether that is correct or whether there are some organisations omitted. If you feel that the landscape is complete, organise a meeting with all the organisations.

But, that is the situation "on the paper" and what interests us more is the real situation, what happens in practice. Our role is not to evaluate their activities, but on another side we cannot close our eyes. Often organisations have beautiful declarations and mission statements but in reality the quality, and sometimes the quantities, is not that impressive. To a certain extent we have come across such differences during our interviews and when reading the documents:

- *On paper:*      *Our credit programme is open to micro producers*
- *In reality:*     *Up to now only three 3 credits were granted*

It is obvious that the micro producers have access to credit 'on paper' but in reality don't use or don't have access to this credit programme. In such a case we have to investigate this discrepancy: or the micro producers are not interested in credits, and as such our analysis might not be correct, or there are certain limitations in obtaining credits, e.g.:

- "the micro producers don't succeed in offering collaterals of \$25.000"*
- "we have a limited portfolio of \$1000 per year"*
- "the process is rather centralised and approval of credits takes roughly one year"*

It is already obvious that the conditions of the organisation are not 'the most appropriate' and we can conclude that in the reality the organisation does not satisfy the identified needs. These observations you also enter in the mentioned schedule under "observations".

When you do think the landscape is complete, organise a meeting with all the organisations and invite a representative sample of your own target group, which is probably also part of the client group of these organisations.

Introduce your findings to the group. Discuss your conclusions concerning the organisational landscaping and in first instance verify whether your findings are correct (facts). Thereafter discuss the operational aspects of the activities of these organisations. This implies that the organisations *and* the producers give their point of the view on these activities (opinions). It is of utmost importance that you as a group, and possibly of you as a chairman of the meeting, do not involve yourselves in a 'yes or no' discussion, but simply find out what the real situation is with respect to the operations of these organisations and your target group. Yet, it would be ideal if the meeting would achieve consensus on a list of strengths and weaknesses, including a list of recommendations to improve them.

Such a meeting is often an eye opener for the organisations involved and it might stimulate more exchange of information or even cooperation among them.

## **5.2 Interventions**

## 5.2 Interventions

### 5.2.1 Introduction

There are dozens of interventions that one can think of that might improve the performance of the sub sector. Yet, which one will be the most appropriate will depend on the actual situation: the structure of the sub sector, its bottlenecks and the opportunities. There are no blueprints: what might be a good intervention in one place might not work at all somewhere else. The best interventions are tailor made to address special needs, they are the logical result of a sub sector analysis.

Nevertheless, there are some *best practices* that are based upon experiences made in various sub sectors all over the world. There is no need to reinvent the wheel so let us learn from those experiences.

### 5.2.2 Principles

Until recently, many NGOs focussed on the various needs of the population and were active in various fields, ranging from humanitarian aid to good governance activities. However, there is a huge difference between humanitarian aid, general structural development and this special field of development.

We as a team or as an organisation can not improve the performance of the sub sector: we can only design interventions that allow the SMEs *themselves* to improve performance! It is up to them!

The SMEs themselves often know best what they need and what they can: they are entrepreneurs! That implies that we should design interventions that are **demand led**. If we offer training, than they should be queuing up to benefit from such courses and there should be no need to force them to participate. If the latter is the case, the intervention is not the right one. That also implies that we should be **business like** in our intervention logic: if the SMEs really want to be trained, than we should ask them to pay for such training: it will not only "fit the entrepreneurial culture" but at the same time indicate their willingness to pay. Being business like in the intervention itself also opens the door for that intervention to be **sustainable**: there are only rare situations whereby we can accept that an intervention is not sustainable in the long run: one day the donor will no longer be willing to pay for the intervention and then it will end!

The best approach for sustainability is coupled with **maximum outreach**: the higher the number of people that will benefit from the intervention, the cheaper the cost per beneficiary and the bigger the impact of our intervention. So we put emphasis not only on maximising outreach, but we also focus on reducing the costs. We opt for the most effective and efficient option and that implies we pay attention to the **cost structure**. Efficiency and effectiveness can only be realised, and measured, if we pay attention to proper indicators, assessments and evaluations. If we design interventions for our SMEs using the above principles, we should be asking them what they need and want: so we don't design *for* them but we design *with* them: we take a **participatory approach**.

- *Hereafter some cases are presented: read them, analyse the core problem and design an intervention according to the principles: be creative!*

### 5.2.3 Metalwork

The main problem for most of the metal workers in A was the lack of equipment. There was a thriving industry before the war, but due to the long and severe war, most of the equipment got lost. The resident metalworkers who had fled the region, returned to their homes and most of them only carried a few hand tools. They lack the main machinery simply because they are not available in the region. Previously that equipment used to be imported from abroad.

A market research was undertaken and showed that there was a market for the products previously produced by these metalworkers. Although there were some imports, these were of a poor quality but yet at a high price. In short, the conclusion was that there was an opportunity for the sub sector, if they only had the means to produce.

➤ *What would you advice?*

### 5.2.4 Furniture

The micro enterprises in the furniture sector in B were losing their market share to importers of furniture and a few larger furniture companies. A market research showed that the products of the micro enterprises were much cheaper and that they were tailor made to the clients needs (specific design wishes).

Yet clients were unsatisfied about the quality of the product: it looked nice but wrapped and cracked after sometime. Moreover, delivery times were long. All of these reasons pointed to the lack of properly seasoned timber: carpenters had little working capital and only bought timber once they had secured orders.

➤ *What would you advice?*

### 5.2.5 Fruits

In C small farmers faced a problem of very unstable and varying market prices. Most farmers produced the same vegetables and fruits that became available on the market at the same time. Only in the pre- and after-season prices were reasonable, while in the high season a considerable part of the produce were sold below the cost price. Traders from other regions came and bought these surpluses at extreme low prices from the producers and sold it to major food processors.

Local traders imported these products again in the off season since there was a constant local demand. The added value was in the food processing, but little capital was available for such an industry. Viability of such an industry was doubtful since the supply was seasonal and rather limited. The small producers were not organised.

➤ *What would you advice?*

### 5.2.6 Vegetables

In D vegetable producers were facing a similar problem: surplus supply dropped the price on the local market in the high season. Traders from other regions came and bought part of these surpluses at extreme low prices from the producers. They sold them to major food processors who exported the processed food. Once every few years there would be less production (poor harvests) and prices would shoot up and little was sold to the traders.

➤ *What would you advice?*



### 5.2.7 Leatherworks

In E the leather worker industry faced the problem of low productivity. Products of a low quality were sold to local customers and the margins were low since they faced competition from imported goods. The number of micro producers also had increased enormously in recent years. Raw materials (goat skins) were easily available and little working capital was required. Since most of the production was manual, no investments were required in expensive machinery.

- *What would you advise?*

### 5.2.8 Informality

In F the micro enterprises were enjoying a high demand for their products. There was little industry that had survived the long war and major (foreign and national) companies were still doubtful whether they should return. The population however had returned and they had limited but sufficient purchase powers: they were in need of various products (furniture, burglar bars, clothing, shoes, pottery) that the micro enterprises could supply. Margins were acceptable, raw materials difficult but obtainable and staff qualified.

Yet, many were operating illegally in the sense that they were not able to comply with all the rules and legislation set by the government. They were exposed to huge penalties or bribes to avoid closure of the enterprise: the total bribe or penalty sometimes amounted to half the profit!

- *What would you advice?*

### 5.2.9 Innovations

In G a sub sector study had revealed that the industry had missed various innovations. The university, having the financial and human resources, was given the lead in training entrepreneurs in getting acquainted with new products and technologies. The entrepreneurs were invited (free of charge) to participate in 5-day-classes once every two months. An evaluation after two semesters was very negative: less than 10% of the initial entrepreneurs participated in the course.

- *What is your advice?*

### 5.2.10 Bread makers

In previous times, bread in H had been produced by the large state company. Soon after the liberalisation the state company went bankrupt due to inefficient production and lack of market orientation. Two other smaller bakers started but they soon faced fierce competition from the micro producers and are now operating at half their capacity. At present, the micro producers face the problem that their ovens are old and rather expensive since they use firewood which is getting more expensive everyday. Many producers would like to switch to gas operated ovens, but with a constant yet low cash flow most of them lack the capital to invest.

- *What would you advise?*

### 5.2.11 An overview

The above cases are some examples of what kind of interventions are possible. We can use the following division to structure these interventions.

- Technology
- Advocacy
- Business Development Services
- Financial Services

Under *Technology* we distinguish between those interventions that train in using the existing technologies and those interventions that develop new products or production technologies. For example, vocational training centres are more focussed on the first while research institutes are typically focussed on the latter. Technical training can be given by public and private schools, but also short courses and informal apprenticeship schemes fall under this heading.

*Advocacy* includes activities that promote the better functioning of the SMEs and can take any form. They are often oriented towards lifting certain barriers and towards legislation. They can be sub sector specific (for example sub sector associations) or more general for the SMEs (for example trade promotion organisations).

*Business Development Services* are non financial services and training is the oldest form and still an important one. Training can focus on entrepreneurship, on business management or on farm management (technical training we included under *Technology*). Besides the training intervention we also list the advisory and counselling functions here: a farmers extension service is a good example. Commercial services (consultants, accountants) are included here too. Another type of intervention are those interventions that focus on market linkages: improving the relation between the producer and his market such as market information systems or contract farming.

The *Financial Services* are those that focus on improving access to capital: working capital or capital for investments. We often structure them according to the clients: micro, small or medium enterprises. Micro credit schemes are a typical example for working capital for micro entrepreneurs, while leasing is one example of financing capital needs of a medium enterprise.

- *Look at the presented cases; where would you list them in the above structure?*

## **Tasks Unit 5**

## 1 Organizational landscaping

What we already have:

- a list of organizations that were mentioned during the interviews.
- a list of organizations that are or might be active in one of the fields.
- a one-page checklist for each organization.

So, the only thing lacking is a plan and a division of the team tasks and then:

- Interview the relevant organisations.
- Process the obtained information and complete the table for the landscape.

The double confrontation:

- Confront the needs with the activities of the organisations
- Organize a meeting with all the organisations and a representation of your target group

## **6 Designing**

## **6.1 From Analysis to Intervention**

## 6.1 From analysis to intervention

### 6.1.1 Introduction

We are now reaching the stage whereby we start designing interventions. Before we do that, let us check what we have accomplished in the past few months:

We have interviewed the SMEs and understand the way they function. We know where they buy their inputs, how they produce and to whom they sell. We know what their successes have been and we know what constraints they are facing. We identified variations within the group of SMEs.

We have talked to their suppliers and we know how that part works. We understand the constraints of the suppliers of the suppliers and we noticed changes in the system. We calculated the costs and know what the profits are.

We surveyed the consumers and we know what they appreciate most: why some products do satisfy their needs and why others don't. We identified various segments and we know all about their wishes, their thoughts and their abilities to buy.

We interviewed (semi-) government institutions and are aware of what the government thinks of our sub sector. We know their policies but we also know the realities. We identified the constraints in the legislation and barriers caused by regulations.

We have had meetings with other organisations who are active in the SME sector. We know what they are achieving and we have learned from their experiences. We know what works and what doesn't. We know who is doing what but we also know what nobody is doing!

We have drawn a map of the sub sector. We know the ins and outs, there are no question marks. We identified all major channels and we calculated the margins in these channels. We estimated the volumes and number of actors in these channels.

We have applied a SWOT analysis on the sub sector. We know the strengths and weaknesses of the SMEs and we identified the threats and opportunities in the environment. Moreover, we identified winning combinations and major challenges.

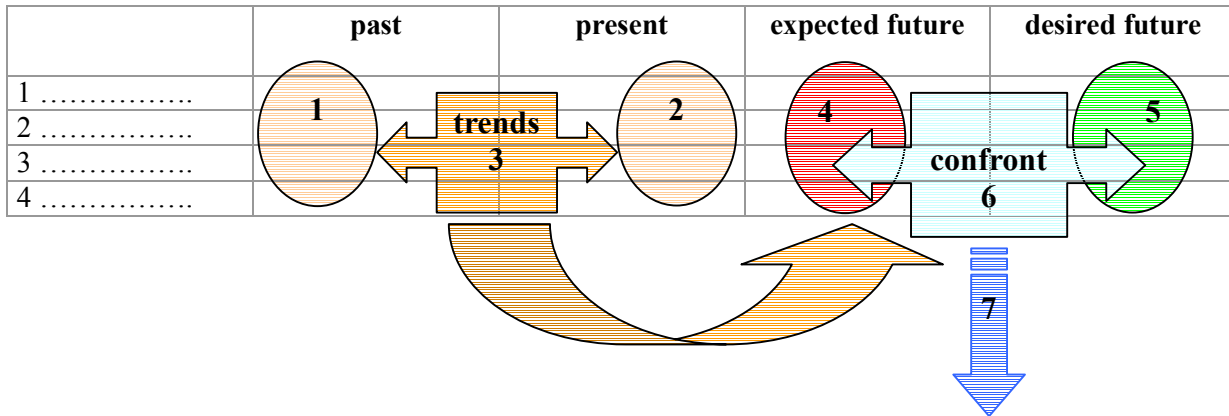
So we can now call ourselves experts! Let us make use of that expertise and design appropriate, effective and efficient interventions that will enable the SMEs to improve their performance.

### 6.1.2 Starting point

Before we start designing the interventions, let us go through the information we have obtained so far and let us go through the conclusions we had already drawn too. We did so at various points in the past few months, but now we have completed the exercise so it might be useful to see if 'all is still correct'.

*Are the conclusions we drew in the first month not contradicted by information we obtained last week?*

A very effective way of analysing and identifying is by writing down how certain things were in the past, how they are done at present, how it is expected to work in the future and how we would like to see it work in the future. The information we have obtained so far will assist us in that process, and that process will assist us to crosscheck and verify all this valuable information: we will thus no longer have to search for information, but we now let that information assist us in this creative process!



By comparing the past (1) and the present (2), one easily notices changes, tendencies and dynamics (3). This is especially true when distinguishing between micro, small and medium enterprises. With the identified changes, tendencies and dynamics one can try to predict the future (4).

This expected future is then compared with a future the way would like to see it (5). If we then confront the expected future with our desired future (6), we see what changes are necessary: this is the starting point for our intervention (7)!

The following example might illustrate this:

- Past:** *In the past the retailers bought their products from the larger producers.  
In the past the small producers sold their produce directly in their neighbourhood.*
- Present:** *At present retailers buy cheap products from importers.  
At present there are more retailers operating in the neighbourhoods.*
- Trend:** *The number of retailers increases and they import cheaper products.*
- Predicted future:** *The supply of imported goods increases and small producers lose their markets*
- Desired future:** *Small producers secured of sufficient and profitable market segments*
- Confrontation:** *The small producers cannot compete on price*
- Starting point:** *Interventions that improve competitive advantages of small producers (non-price-competition: quality, delivery, segments, etc.).*

### 6.1.3 Checklist

The list presented hereafter is a summary of key points and for each subject we should:

- describe the past and distinguish between micro - small and medium enterprises
- describe the present and distinguish between micro - small and medium enterprises
- describe the changes
- identify tendencies

The questions mentioned for each subject are no more than a first indication of what type of questions should be asked and answered: in principle again the *what-why-where-when-who-how* questions!



*The target group*

Have we described our target group correctly in terms of definitions? Do we know who they are and who they are not? What distinguishes them from others? Are they true entrepreneurs? What is their number? Are they growing in size?

*The sub sector**Markets*

Are the entrepreneurs operating in a buyers or in a sellers market? Are the markets well known? How many segments are identified? Are the segmentation criteria correct? Which criteria are most decisive? Who is serving which segment? Are the most attractive segments accessible? Where is competition most fierce? What do they compete on? Which segments have restricted access and why? What is the perception of the clients of the SMEs? What do customers value most? What do they complain about? Why don't they buy more? Do they pay cash or on credit? What are the criteria?

*Competition*

Where is competition fierce? What is being competed on? Are products the same? Are there substitutes? Are there imports? What are the differences between imported and locally produced goods? What are the main outlets? What are the competitive advantages?

*Suppliers*

Where are the raw materials procured? What is their importance? Is it a buyers or a sellers market? How many suppliers are there? What is the volume traded? Is supply restricted? What is the major bottleneck? How long is the supply channel? Are there more supply channels? How risky is the supply? What influences the availability? How is the cost structure? Is it capital intensive? Are entry barriers high? What are the margins? Are the raw materials also in demand outside the sub sector? Are suppliers also producing? Are producers also supplying? What technology is used? What are the regulations for them? What are the relevant government policies for them? What is the effect on the environment? How many people are employed?

*Production*

How regular is the production? Is it production or demand driven? Is it on order or for stock? What are the volumes produced? What is production time? What is the lead time? What are the production methods? Is it complicated or easy to copy? Is it transformation or assembly? Is it cost effective? Are there waste products? Is production efficient? Where can savings be made? Where are areas for improvements?

*Technology*

What technology is in use? Is it labour intensive? Does it require capital investments? Where can one buy the technology? Is it expensive? Is it difficult to use? Is it imported? Is it adjusted to local circumstances? Is it state-of-the art technology? Have there been innovations? Is there a servicing industry? Is it efficient? What is the effect on the product? What is the effect on employment? What is the effect on the environment?

*The human resources*

Who are the employees? Are they qualified? Where are they trained? Are they men or female, young or old? How are production circumstances? Who are key staff? Is staff scarce? Skilled or unskilled labour? How are they paid? How are they perceived? Are they a feeding ground for entrepreneurs?

#### *The products*

What are the main products? What are fast sellers? What are the key characteristics? Are they fresh? Can they be stored? How are they packed? What are the qualities? What are the specifications? What are the product variations? Are they traditional or new products? Are they meeting expectations? How do they compare to imports? Are there substitutes? Are there regulations? What are the main production constraints?

#### *The distribution*

What are the channels? Are they long or short? What are the margins in the channels? What are the volumes in the channels? What are the number of actors in the channels? What is the relation between producer groups, channels and consumers? Where is most value added? Are they supply or market driven? What are the functions of the actors in the chain? Are all actors licensed? What are the major bottlenecks? Where are opportunities? Are distributors also producing? Are producers also distributors?

#### *Promotion*

Are producers known to the public? How are they perceived? What is their perception? Where are they located? Is there a regional concentration? What is their reputation? Which promotional tools are applied? What tools could be introduced? What should they promote? How can visibility be improved?

#### *Pricing*

What are the prices? How are they determined? What are the cost prices? What are the variations in costs? What are the market prices? Who are the market leaders? Who sets the price? What is the relation between price and quality? Do prices differ in place or time? What are the margins? What is the relation ship between direct and indirect costs? Can costs prices be reduced? Are scale effects relevant? Can supply costs be reduced? Can market prices be improved? Is there competition on price? Are net profits reasonable? What is the cost of taxation?

#### *The regulations*

What are the official regulations? How are they applied? Are they a constraint for entering? What are the costs of regulating? Are bribes paid? Is there an informal sector? What is the vision of the government? What are the effects of these regulations? If they would change, what would be the effect for the sub sector? What are the chances on changes?

#### *The infrastructure*

Is the energy supply reliable? Are the costs of communication high? Are the conditions of the roads a constraint for transporting goods? Is it difficult to obtain a plot on an industrial area? Are accountants qualified? Are cars and machinery easy to service? Is export difficult? Is security a problem? Is foreign currency restricted?

#### *The networks*

Are entrepreneurs organized? What is their conception thereof? How are they perceived by the government? Are they active? Do they have links outside the sub sector? Are there commercial

relations between the entrepreneurs? Is there commercial cooperation within the sub sector chain? Are there business relations with other companies outside the sub sector?

*Macro economic factors*

What are the prospects for the local economy? How does that effect the sub sector? Is inflation high? What are the purchase powers for the population? Is diversity in purchase powers expected? Is the exchange rate stable? What are the policies of the government? What are the visions of the donors?

- *List all the important information in the following table. Always ask yourself whether the information is correct and complete!*

	<i>past</i>	<i>present</i>	<i>changes</i>	<i>tendencies</i>
<i>Markets</i>				
<i>Competition</i>				
<i>Suppliers</i>				
<i>Production</i>				
<i>Technology</i>				
<i>Products</i>		Micro Enterprises		
<i>Distribution</i>		Small Enterprises		
<i>Promotion</i>		Medium Enterprises		
<i>Price</i>				
<i>Regulations</i>				
<i>Infrastructure</i>				
<i>Networks</i>				
<i>Macro economy</i>				

#### 6.1.4 The criteria

Now that we have updated and completed our information on the sub sector, we should refer once more to the criteria set earlier. In unit 4.4 we set a few economical criteria and you as an organisation might have added other criteria. We should again check whether the sub sector justifies our interventions: does the sub sector have potential? What are the possible effects on employment, added values, volumes, self sustainability and what is the government policy?

- *Check the criteria for the sub sector*

### 6.1.5 The analysis

We have already applied a SWOT analysis at an earlier stage but we need to check whether the outcome is still correct. Now that we are experienced in that tool, the update will not be that time consuming. We check the major strengths and opportunities and the major weaknesses and threats, where after we order them in winning combinations (SO) and major challenges (WT).

- *Decide whether the identified issues are strengths, weaknesses, constraints or opportunities*

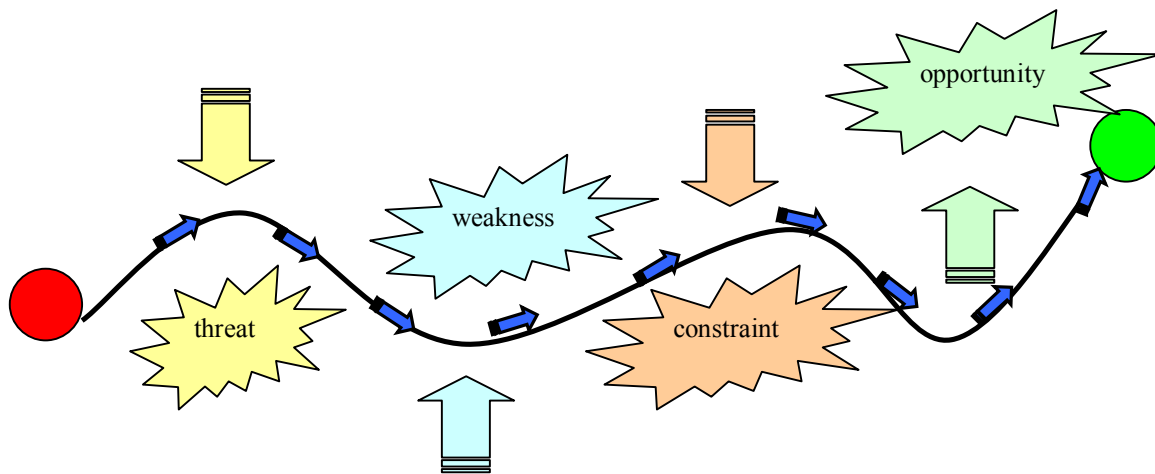
	<b>Positive</b>	<b>Negative</b>
<b>Internal</b>	Strength	Weakness
<b>External</b>	Opportunity	Threat

*Markets  
Competition  
Suppliers  
Production  
Technology  
Products  
Distribution  
Promotion  
Price  
Regulations  
Infrastructure  
Networks  
Macro economy*

- *Define the winning combination and major challenge*

### 6.1.6 The strategy

At this point, we have a rough idea about the position the SMEs are in and the direction they should take to improve their position:



We probably have an idea about the path (the strategy) the SMEs have to take from the red position (left) to the green position (right) and what their problems might be on the way: we thus design our interventions (the arrows) to address these constraints. *The SWOT analysis provides us with the strategy!*

*We now ask ourselves two questions:*

- 1 what are the constraints they (might) face implying that strategy?
- 2 what would be the best intervention to address these constraints?

### 6.1.7 The interventions

There are many solutions to a problem:

*If you can't find a certain shop in town you can:*

- *walk until you find it,*
- *ask somebody to show you how to get there,*
- *take a taxi and be driven there.*

There are thus many interventions that might be appropriate for your sub sector SMEs. The best intervention is the one that addresses the cause of the problem and not the problem itself:

*Problem: The SMEs have no capital to buy modern equipment*

*Solutions: Provide equipment or  
Provide capital*

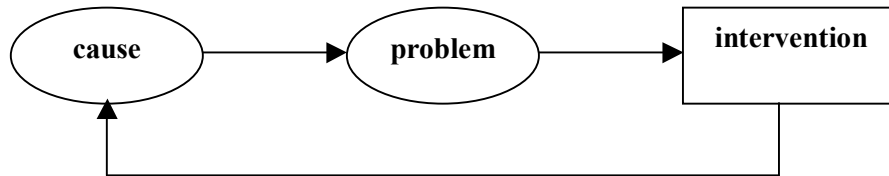
These solutions do not resolve the problem: they might relieve it for some time, but the problem will not be solved.

*The equipment will be used but when it is worn out they again will have no equipment*

We must therefore focus on the cause of the problem:

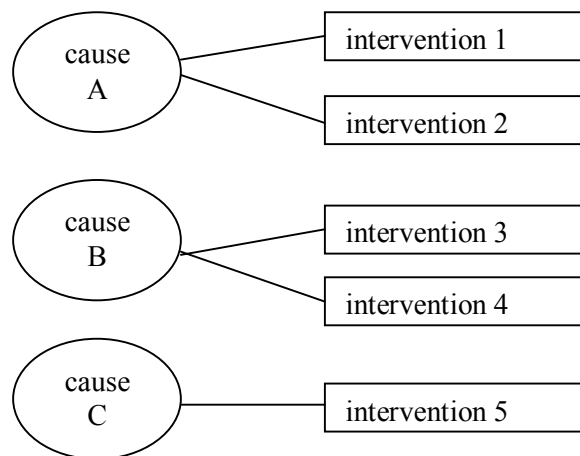
*Cause: Margins were too low or  
SMEs have eaten their profits*

*Intervention: interventions that improve the low margins  
interventions that change the attitude of the SMEs*



With this principle in mind, we check our overall strategy (the SWOT outcome) and identify the causes of each constraint: the weaknesses and the threads, but also the other constraints that need to be tackled on the way, and how to reinforce the strengths and enlarge the opportunities.

With this logic, we design interventions that address the identified constraints. The result will be that we have a certain number of "causes" and a certain number of "interventions". We must then choose the most effective intervention. Not only will we not be able to implement all interventions for practical reasons, but we must also check our intervention principles.



- *Verify whether the interventions address the underlying causes and not only the identified problems.*

### 6.1.8 Check on principles

We confront each intervention with the principles:

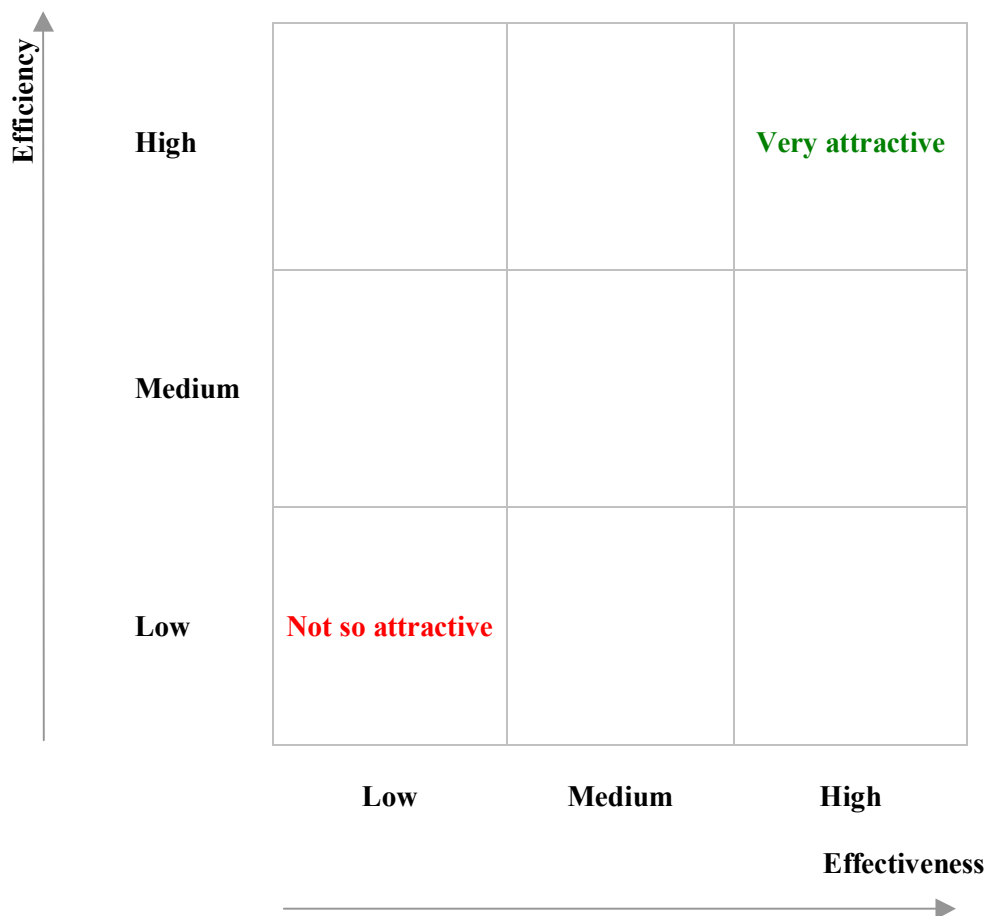
- is the intervention demand led?
- is the intervention business like?
- is the intervention sustainable?
- does the intervention maximise outreach?

➤ *Confront each possible intervention with the above principles.*

Thereafter, we remain with a reduced list of possible interventions and we have to select the most effective and efficient intervention, whereby:

effectiveness: most chances on realising the desired objective  
 efficiency: the costs per beneficiary are lowest

We may use the following schedule to make that comparison and selection:



In the following example we compare five possible interventions:

<b>Efficiency</b> ↑	<b>High</b>	<b>Intervention 2</b>	<b>Intervention 5</b>
	<b>Medium</b>	<b>Intervention 3</b>	
	<b>Low</b>	<b>Intervention 1</b>	<b>Intervention 4</b>
		<b>Low</b>	<b>High</b>
		<b>Effectiveness</b> →	

Intervention 2 appears very good in terms of efficiency but scores low on effectiveness.

Intervention 4 is low in terms of efficiency but is very effective.

Intervention 5 scores well in both aspects: high in terms of effectiveness and high in terms of efficiency.

It is important to concretise the defined effectiveness and efficiency for each intervention:

*Intervention 1 is a visit by five micro producers to a neighbouring country to familiarise themselves with a few new technology.*

Intervention 5 implies the participation of 25 micro producers in the local trade fair to improve the linkages between the producers and the market.

The efficiency of the first intervention is low because the cost per beneficiary are high while the impact of the intervention is not that clear: do the producers have the capacity to apply the new technologies?

The efficiency of the fifth intervention is higher because the cost per beneficiary are less and the impact appears much higher and direct: a concrete result in a short time span.

- Order your identified interventions in a similar table and choose the most efficient and effective intervention.



### **6.1.9 Verify the organisational landscape**

The landscaping exercise has provided us with information about the fields, expertise and activities of other actors. We check whether there are organisations already implementing this type of interventions and if there are, we share our knowledge with them. They might improve their existing intervention. We then check whether it is still justified to implement the second best intervention.

If there are no organisations implying such interventions (the gap), we check whether there are organisations that would be suitable to implement or co-implement this intervention. In such case, we can start writing the intervention proposal together. If not, we have to verify if we are in conditions to implement the intervention ourselves.

### **6.1.10 The next step**

At this moment we have a rough idea about the intervention and the constraints, objectives, target group, methodology, activities and expected results. So, we have to develop a well structured project document. For this, we will make use of the Logical Framework Approach when we work out the intervention in the following and concluding module.

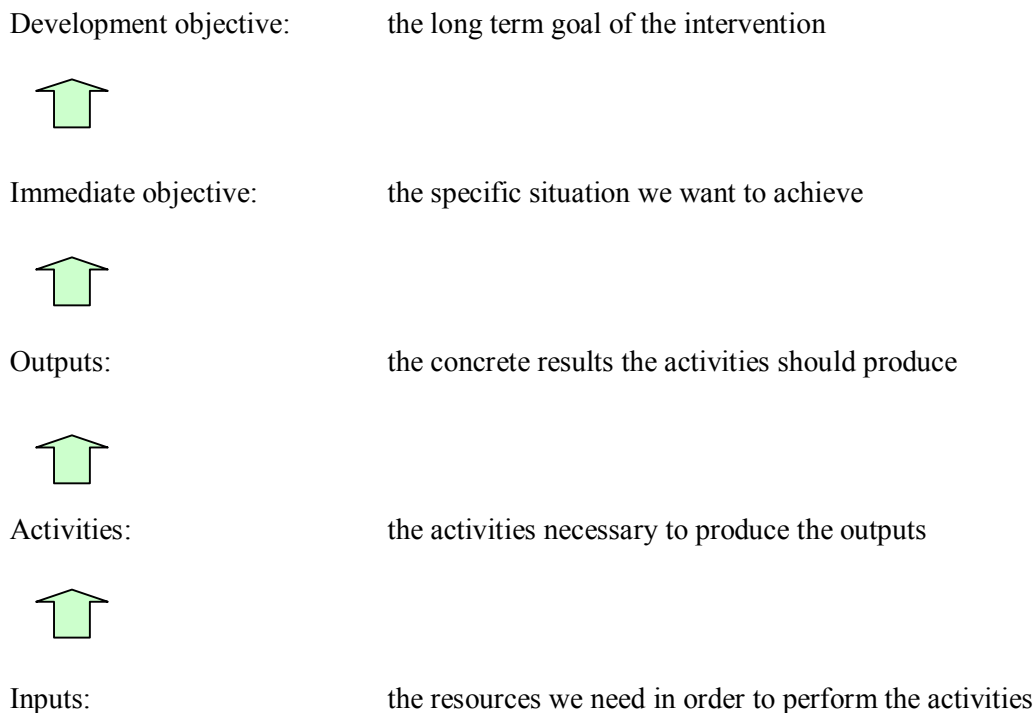
## **6.2 Logical Framework Approach**

## 6.2 The Logical Framework Approach

### 6.2.1 Introduction

The Logical Framework assist us with the design of the project. With this tool we can easily order the elements of the intervention in a logical structure. Usually the donors request that the logical framework is included in the project document.

We specify concrete objectivities that the intervention should achieve. We therefore decide what the concrete results of activities should be and decide on concrete activities. Inputs that are necessary to perform activities are then identified.



### 6.2.2 The structure

#### The development objective

The development objective is the overall objective of the intervention that can not be achieved by the intervention alone but to which it contributes significantly. It is of a higher level than the immediate objectives:

*e.g. . sustainable access to safe water*

The intervention alone cannot guarantee access to safe water but the immediate objectives can contribute to that overall objective. The development objective is rather general and describes the ideal situation in the long run.

## The immediate objectives

The immediate objectives describe the desired situation at the end of the project period as a direct result of the planned intervention.

*e.g. increased and continuous supply of piped water*

However, the immediate objectives should be specific, measurable, accurate, realistic and time bound (SMART):

*e.g. financially and technically sustainable, uninterrupted supply of save water (30 litres per capita per day) for 2230 households in North Western Province by December 2004*

## The outputs

The outputs are the direct results of the interventions. It is always difficult to distinguish between objectives (that what you want to achieve but not in your control) and outputs (results that are the result of the activities under your control):

*objective: population has adequate hygiene practices*  
*output: awareness campaign about hygienic practices conducted*

It is of course possible to design various outputs to achieve one objective and therefore you must number the outputs. Describe them as detailed as possible: the more you try to specify them, the more it will help you to focus when designing appropriate activities.

*objective: increased and continuous supply of piped water*  
*output 1: 200 new connections ....*  
*output 2: 40 existing pumps rehabilitated ...*  
*output 3: 80 committees ..... etc.*

## The activities

The description of the activities should reflect the methodology, the approach, and should thus be as detailed as possible, preferably broken down in various sub activities (steps):

*output: 1: five trained pump mechanics*  
*activity 1.1: identify training needs*  
*activity 1.2: develop participatory course*  
*activity 1.3: implement course*

We thus design the activities according to the desired results (outputs), which is the opposite of designing activities and than imagine 'what the results might be', a practice often applied! The output reflect the end-situation, the activities reflect actions, steps, the process to get there.

## The inputs

The inputs are the resources needed to perform the activities: human resources, equipment, materials and premises. They all have a cost. However, the inputs need to be specified (quality, quantity) both in non-financial terms and in financial terms (budget).

### 6.2.3 The matrix

We can now apply the above elements in a matrix and include indicators, assumptions and preconditions:

Elements	Indicators	Assumptions
Development objective	<i>Indicators</i>	<i>Assumptions</i>
Immediate objective	<i>Indicators</i>	<i>Assumptions</i>
Outputs	<i>Indicators</i>	<i>Assumptions</i>
Activities	Inputs	<i>Preconditions</i>

**The assumptions** are events, conditions or decisions that are not under the control of the project but that may influence the project. If they are important and relevant we write them in the last column: we will be alerted to look out for such events. Assumptions are related to the levels: the first level are those that relate to the step *activity-output*; the second level those that relate to the step *output-immediate objective* and the top level relates to the step *immediate objective- development objective*.

**The preconditions** are then of course the conditions that need to be met before the project can be initiated.

*outputs: village committees trained ....*  
*assumption: sufficient number of interested and suitable villagers can be identified*

In the second column **the indicators** need to be stated. These verifiable indicators should be as specific, measurable, accurate, realistic and time bound as possible, in order to monitor and evaluate the project. They are thus necessary for each objective and output:

*output 4: provincial offices able to register village committees*  
*indicator 4.1 no more than 5 complaints received during 2003 over inability*

- Design your intervention using the Logical Framework

## **Tasks Unit 6**

## 1 Logical Framework:

What we have achieved so far:

- We have interviewed the MSMEs.
  - We talked to their suppliers
  - We know the consumers.
  - We interviewed the (semi) governmental organisations
  - We held meetings with other organisations
  - We drew the map of the sub sector
  - We applied a SWOT analysis of our sub sector
  - We identified the changes and tendencies
  - We verified the criteria for the sub sector
  - We applied a final SWOT
  - We confronted the needs with the offers by the organisations during the landscaping exercise
  - We confronted the identified interventions with “the principles”
  - We ordered the interventions and selected the most appropriate interventions
  - We have chosen our intervention
  - We designed the most appropriate strategy for this intervention:
    - The principle objective
    - The target group
    - The methodology
    - The activities
- Make the Logical Frame

<b>Elements</b>	<b>Indicators</b>	<b>Assumptions</b>
Development objective	<i>Indicators</i>	<i>Assumptions</i>
Immediate objective	<i>Indicators</i>	<i>Assumptions</i>
Outputs	<i>Indicators</i>	<i>Assumptions</i>
Activities	Inputs	<i>Preconditions</i>

- Write you proposal!