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BOOK REVIEWS

Ernst A. Brugger and Sarath Raja Datirana (editors), New Perspectives on Financing Small Business in Developing Countries, (1995), pp. 194, n/p.

The book under review is a collection of papers read at the workshop jointly sponsored by the Latin American Technical Department of the World Bank and Fundacion Para of Desarrollo sostenible (FUNDES) held in Washington, DC., in October 1992, along with some other selected papers. It is divided into three parts containing ten chapters. Part I, which provides the knowledge of basic problems faced in financing small businesses, presents the conceptual framework. It also highlights the issues relating to the accessibility of small enterprises to conventional sources of financing.

Part II contains the most practical part. It covers fifty per cent of the book, and deals with the empirical evidence and case studies. The approach is simple and fancy econometric techniques or sophisticated modelling is not used; evidence are provided in the form of tables. The author draws some policy conclusions in Part III, regarding financing of small businesses in developing countries based on assessments in the earlier parts of the book.

Doug Salloum estimates that about 50 per cent of the population in developing countries owe their survival to the informal sector followed by the fact that the small businesses contribution to economic activity is as high as 90 per cent. Following this all the authors focus on the importance of small enterprises.

The author Ernst A. Brugger, one of the editors of the book, raises an important point based on the assumption, that small businesses are crucial to the development process in developing countries. On page 177 he states that "Small business sector is the only economic mechanism capable of generating sufficient wealth to allow millions of people at all levels of the society in Latin America, Asia, Africa and Central Europe to break out of the vicious circle of poverty in which they are locked." He argues, that the importance of small businesses is ignored by too many decision makers in politics, banking and the economy. Hence, it is subject to more constraints than it can withstand. This argument needs to be given more consideration by policy makers in developing countries.

It is observed that despite the financial reforms that have taken place in the countries under review, there are still regulations that restrict small companies' access to formal credit. Economic instability and uncertainty caused by constant policy shifts also restricts the profitability of the companies, consequently limiting prospects for expansion.

The problem of sustainability has become a central issue in developing credit systems for small enterprises as pointed out by Nanno D. Kleiterp in chapter 4. He observes that very few examples of sustainable credit institutions exist in these countries.

In chapter 7, Richard M. Hook provides some interesting conclusions based on the experience of Bank Rakyat Indonesia, (BRI) in developing its small scale banking activities. On page 120 the author comments "It (the bank) has demonstrated that it is possible under favorable conditions, to lend money safely in the rural and small business sectors, at rates that produce attractive profits, and at the same time assist in the improvement of income levels and employment." The favorable conditions include supportive political environment, successful macroeconomic management, and population density. But these pre-conditions or favorable conditions do not prevail usually in many developing nations. Only where the basic factors are favorable, BRI's experience is transferable.

Chapter 9 on Role of Saving in Developing Sustainable Commercial Financing of Small and Micro Enterprises is a mere repetition of the experience of Bank Rakyat Indonesia, mentioned in chapter 7 with some elaboration and additional statistics from other developing countries.

Authors Eduardo Lizano and Luis Mesalles present the case studies for Bolivia, Chile, Columbia and Peru, where FUNDES has set up a credit program. This choice according to the authors reflects the different levels of financial sophistication found in Latin America. However, a common factor among these four countries is the introduction of financial reforms during the past few years, which has diminished government intervention in the distribution of funds through official financial system. Though the authors have highlighted different aspects of the problem, they have totally ignored the demand concentrating only on the supply side of the credit. They have also highlighted the fact that since both private and public owned banks operate in the financial market, with the main objective of maximizing profit, small enterprises' access to credit is limited due to the high interest rate charged by commercial banks. Another common reason for lack of development of small enterprises is the economic and political instability that characterizes most Latin American countries.

It is worth mentioning here the experiences of Kenya Industrial Estates Limited (KIE) which helps small business industries. All these small business industries contribute to strengthening the Kenyan economy. KIE has pooled money from the government of Kenya, Germany and Scandinavian countries for lending to small businesses. It is like a bank and give loans to people who rent space in the Industrial Estates. The borrowers put some money of their own to assess the venture's profitability and conduct cash flow planning for their businesses. Loans do not have to be repaid for six to ten years. KIE also provides technical assistance. These businesses generate substantial jobs and produce goods at prices that many Kenyans can afford. The authors conclude that KIE has helped development of small businesses quite significantly [World Bank, (1981)].

Another example is of the Grameen Bank which basically provides credit and organizational help to the poor. It also promotes social development by making the poor individually and socially accountable. This helps in improving their loans repayment capacity and, hence, contributes in Grameens financial viability. Banks loan recovery rate has consistently remained above 90 per cent in case of the Grameen Bank. The loans are also used to finance small businesses in rural areas, and is a great success. [Khandkar, et al., (1995)]. In view of these successful examples from the two developing countries, banks in other developing countries can adopt these models to finance small businesses.

The common costs that generally occur in any inefficient economic and political system are high capital cost, high cost of technology, high administration and legal costs. These push up the unit costs significantly. High transaction cost also discourage investment, risk taking and eventually growth and development as transactions eat up the greater part of the money available. It is observed that due to these problems in most of the developing countries, in spite of massive entrepreneur talent and initiative very little potential is actually realized. Consequently, as most of the new capital markets are not yet competitive, banks are not ready to take highrisks.

Ernst A. Brugger concludes by saying that there is no trade off. This leads to one simple and logical conclusion that the reserves we put at the disposal of the small and micro business sector should be seen as an investment in an open social market economy.

The book is one of the very few on this topic which deals with the issues of the financing of small business enterprises in developing countries. It is educative and should be useful for banks and other financial institutions which deal with the issue of financing small businesses in developing countries.

The book contains a good collection of papers providing insights into one of the burning issues of the 80's and 90's. It also provides theory and practical experiences along with the case studies of Latin American countries reflecting as the specific problems of development policy.

The book has a useful bibliography at the end of each chapter followed by the index in the end. While it offers the experience of some of the Latin American countries, this book, however, falls short of some examples from other developing nations.

The book is a useful quick reference for the finance and business personnels and students working in this area.

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References

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Suraj B. Gupta, Black Income in India, (Sage Publication India Pvt. Ltd., New Delhi, 1992), pp.187, Rs.215.00.

Professor Suraj Gupta, in his book "Black Income in India" mentions that in Indian economy the significant and the fast growing component of parallel economy deserves more attention of the economists/ scholars, than it has received so far. He has made an attempt to bridge this gap by writing this book. The book tries to cover all sources of Black Income rather than emphasing on one or two. Before, publication of this book, most of the literature on black economy in India, pivoted around income tax evasion.

The book consists of 7 chapters. The introductory Chapter 1 is followed by Chapter 2 which is on political corruption and black income. In this chapter the author has argued that to evade tax a macro environment prevailing in an economy is much more important than the individual propensity. This is based on the assumption that black income activities need patronage as well as protection of political leaders and administrators, which is gained through suitable bribes. Political corruption is determined by social structure, state intervention, high political anomie and contribution to party funds.

In chapters 3 and 4, sources and methods of black income are discussed. In chapter 3 evasion of income tax, and excise and custom duties are specifically discussed. In the methods of income tax evasion the author has discussed the role of tax expenditure and tax avoidance in tax evasion, along with many common methods of tax evasion i.e., over statement of expenditures, fictitious dealing, clubbing, trust and gifts. In excise duty, evasion, multiplicity of rate, exemption and specific duties are discussed. In custom duties, misclassification, smuggling, and under-valuation are discussed. Similarly, in Chapter 4 smuggling, real estate, narcotics, mechanism of evasion have been discussed. These two chapters have nothing unique to discuss except efforts of the author to gather at one place the theoretical and practical information on issues of tax evasion, which must be appreciated.

Chapter 5, on estimating black income in India, is supposed to be the most important chapter of the book but turns out to be the most disappointing part. In this chapter the author has conspicuously failed to leave a good impression. In this chapter the author try to improve the ball park estimate of the National Institute of Public Finance and Policy (NIPFP) by a set of different factors based on his own judgement. For example, in case of evasion of income tax the author second the NIPFP estimates; but assuming that over the tax, the evasion has become progressive, it increases the ball park estimate by almost 10 per cent. In case of corporate tax he assumes that evasion is around 30 per cent of the actual tax collection, as compared to 25 per cent as assumed by NIPFP. In case of custom duties the book assumes 30 per cent evasion and for excise duty 40 per cent. Similar ad-hoc assumptions are made for other heads of evasion.

In Chapter 6, Professor Gupta discuss the political, social, and economic consequences of black income. He argues that the black income distorts income and wealth distribution; has adverse implications for monetary and credit policies; increases budget deficit, and hence leads to inflation. It also distorts the data base and in turn affect projects for future planning. The author argues that economic consequences of black income leads to political pressure, create power groups and finally tends to change the social structure of the society. In Chapter 7 the author has also reviewed the measures to deter tax evasion and measures to unearth black income. However, he states that despite all these efforts the government has failed to unearth black income in India.

Overall, this is an interesting book and covers almost all theoretical and practical methods of evasions of taxes. However, it has two major deficiencies, first, it tries to cover almost all issues of black income, therefore no justice is done to individual topics and in most cases it is only able to give cursory treatment to them. Secondly, Prof. Gupta did not use any scientific, monetary, fiscal, and accounting techniques to estimate black income in India. In this regard he tries to improve the ball park estimate of NIPFP by his own presumption, which makes the book less useful for academician and scholars. This book might be of good use for policy makers in India and is definitely a good reference for students of Public Finance.

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