

# Approved But Not Contracted: Assessing the Challenges of Women Owned Small and Medium Enterprises Integration into the Formal Economy in Malawi

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**Abstract:** Women economic empowerment has become an established policy goal in a number of countries. There is currently increased belief that this goal can be achieved by supporting small and medium enterprises (SMEs). To this end, restructuring of economic activities to facilitate women participation in the formal economy is seen as a sure way to developing SMEs. Integration of women owned SMEs into the formal economy is particularly perceived as facilitating women owned SMEs access to investment capital, business and market opportunities. The process of facilitating new entrants into the formal market, however, involves negotiations and contestations among market actors. Employing the social capital concept, this paper examines the challenges of women integration into the formal sector in Malawi. Data for this paper was collected through structured interviews and focus group discussions with women owned SMEs. The study findings demonstrate that unless accompanied by enforcement mechanisms, women integration into the formal economy will remain symbolic than real. While there is a lot of rhetoric for the integration of women owned SMEs into the formal economy, formally registered women owned SMEs largely survive through informal transactions. In particular, the findings demonstrate that bridging social capital that enables entrepreneurs to operate in the formal economy is locked out for many women forcing them to depend on informal bonding social capital.

**Keywords:** Women SMEs, Malawi, Social Capital, Integration, Institutional Enforcement

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## 1. Introduction

This paper undertakes a critical review of the challenges women owned Small and Medium Enterprises (SMEs) face in getting integrated into the formal economy in Malawi. The paper responds to the emerging literature that presents SMEs as a solution to achieving national economic development and women economic empowerment [13], [28]. Generally, the proposition that SMEs are a potential catalysts for national economic growth and women economic empowerment is attractive for Malawi as the country struggles with low economic growth and increasing poverty among females. Existing data for Malawi shows that SMEs contribute about 3% to the country's GDP and over 80% of women entrepreneurs operate in this sector [15], [23]. In other countries, however, SMEs constitute an important proportion of the country's

economy. According to Peters [39], in Kenya, SMEs generate 12-14% of the national income. Thus, the Government of Malawi see development of SMEs as a tool for reducing poverty and increasing peoples' incomes, especially among women [23].

Generally, policy shift towards developing SMEs is justified on the unimpressive development outcomes of the 1980s development approaches. In particular, a number of scholars have criticized the 1960-80s modernization development paradigm as being responsible for feminization of poverty [1], [37]. The argument is that modernisation development approaches were not only western biased, but also promoted masculine business structure [30]. Poverty statistics for Malawi, which has faithfully implemented modernization approaches for years, attest to this argument. While 59% of female-headed households in Malawi are poor,

the proportion of poverty stricken male-headed households stands at 51% [47]. Consequently, there is an increasing position that promoting women owned SMEs, rather than large enterprises is a surest way of achieving inclusive economic growth and development in a country where women make up 52% of the country's total population [23].

Current policy shifts towards promotion and integration of women owned SMEs into formal economy in developing countries must, however, respond to the fact that actors integration into any institution is not a neutral free process. Instead, the integration process involves negotiations, contestation, rejection and approval [49]. This situation poses two dilemmas that current efforts of integrating women owned SMEs into the formal economy must respond to. Firstly, contrary to the view that women are passive economic actors, women have a long history of participating in the informal economy. Existing studies emphatically indicate that, though characterized by little profit margins and low growth potential, a greater proportion of women are already operating informal businesses [14], [32]. Secondly, women concentration into the informal sector is not an accidental occurrence, but a well calculated survival tactic dictated by social, economic and cultural barriers that limit their participation in the formal economy [3], [8] [36]. Thus, the most debatable aspect of facilitating women owned SMEs integration into the formal sector concerns the extent to which current initiatives will overcome challenges that have for a long time pushed women entrepreneurs into the informal economy.

Employing the lens of social capital concept, this paper responds to these questions by examining the challenges of women integration into the formal sector in Malawi. Using the case of Blantyre City, the study's crucial questions are; what are the new sources of investment capital, managerial skills and market opportunities accessed by formally registered women SMEs? what are the new types of businesses that women entrepreneurs have adopted as a result of their integration into the formal economy? and what barriers and limitations do women owned entrepreneurs face in accessing investment capital, managerial skills, business and market opportunities? In general, this study therefore examine the barriers that limit women successful integration into the formal economy; as measured by the ability to access investment capital/credit capital, business managerial skills and business and markets opportunities.

There is a growing literature on SMEs internationally and locally that highlight the difference between men and women owned SMEs [14], [34]. Generally, these studies have pointed personality and cognitive characteristics that determine performance of SMEs [6], [22] [25]. However, these studies implicitly assume that men and female are operating in the same formal market structure. Current studies have particularly not responded to the fact that most women owned SMEs are operating in the informal sector [11], [12] [32]. Thus, the debatable subject at hand relate to challenges women are facing in getting integrated into the formal economy. This is the gap that this paper aims to fill.

### ***1.1. Conceptualizing Women Owned Enterprises***

There are varied and at times confusing definitions of the term SMEs. According to Appiah-Adu and Singh [4], SMEs are businesses with higher resource limitation in terms of finance, management, manpower market share; and have flat, flexible structures and research credits. However, definitions of SMEs differ from country to country and an SME in one economy could be defined as a micro enterprise or medium enterprise in another economy. For instance, a firm that employs up to two hundred and fifty workers is considered an SME in United Kingdom while in Kenya a business with up to fifty workers is categorized as a SME [39]. In Malawi, a SME is defined as an enterprise which employs between five to twenty people and has an annual turnover of between US\$500 and US\$14, 000 [23]. There are also variations over the conceptualization of women owned SMEs. In Malawi women owned SME is defined as an SME which has 50% or more of the business owned by a woman, employs a maximum of 20 people, and has an annual turnover of US\$14, 500. This is the definition adopted by this study.

### ***1.2. Theoretical Context***

There is an increasing body of literature that explain the role of social capital in affecting the performance and development of SMEs [29], [46]. World Bank [48], particularly presents social capital as the missing link in economic development, including development of SMEs. Social capital can be defined as the aggregate of the actual or potential resources which are linked to possession of a durable network of more or less institutionalized relationships of mutual acquaintance and recognition [7], [16], [18]. According to Putnam [40], social capital originate from norms, networks, and relationships of the social structure in which an individual is embedded. With regard to business, social capital enable individuals access business information, facilitate mutually beneficial trades, resolve collective action problems and reduce monitoring and transactions costs [17], [45]. The argument is that individuals with adequate social capital benefit than those without adequate social capital. These aspects are critical factors affecting both development and performance of a business [24], [36]. Social capital is a strategic resource for women entrepreneurs as it either facilitates or bars their access to investment capital, business and market opportunities and managerial skills. Thus, social capital is one of the determinants of business performance [44]. For instance, Perrault et al [38] found that Chinese, Italian, Indian and Jewish businesses perform well due to the high social capital present in their groups.

Social capital is, however, not a magic proof in promoting individuals' interaction and integration. This is so as different types of social capital operate at different levels of society organisation and structure. Bonding social capital operate at micro-level community while bridging social capital operate at macro level community. Generally, actors in informal business sector use bonding social capital while actors in formal business sector use bridging social capital. The

dilemma for women integration into the formal business sector then zeros down to the extent to which they will successfully acquire the bridging social capital to operate in the formal sector.

Equally important, social does not always lead to positive outcomes. Instead of increasing access to information, it can close other people from accessing information, divide rather than unite people and bar other people from social inclusion and mobility [43]. For instance, Zuka [49] found that social stratification in communities of two irrigation schemes in Malawi led to inequitable access to land and irrigation water. He concluded that social capital does not necessarily lead to good outcomes for all members concerned, rather the beneficiaries are those occupying powerful positions and those supporting the power structure. Likewise, De Filippis [40] also argued that social capital benefits a dominant group in a network or relation but may not benefit others. This consideration is important as women and men are dichotomously embedded in different social networks [41]. It is with this idea that this study adopt social capital to guide its analysis.

## 2. Methodology

This study adopted mixed study approach though qualitative methods dominated due to the nature of the study. The qualitative methods were used to analyze the social and economic contexts under which women owned SMEs operate and the factors that facilitate or bar their integration into the formal economy [10], [19]. Quantitative methods were employed to define the sources of investment capital, managerial skills and market opportunities for women owned SMEs. Primary data was collected through key informant interviews, focus group discussions and a survey of women owned SMEs. The study randomly selected 50 out of 300 women owned SMEs for a semi-structured interview survey. The study further conducted in-depth interviews with 15 women entrepreneurs who did not participate in the survey. Finally, the study conducted 5 focus group discussions with women entrepreneurs who did not participate in the survey and the semi-structured interviews. This sample is adequate to generalize findings for a predominantly qualitative study [33]. The study used content analysis to analyze qualitative data and descriptive statistics to analyze quantitative data.

## 3. Study Findings

### 3.1. Socio-economic Characteristics of Respondents

The study found a convergence in terms of the general socio-economic characteristics of women entrepreneurs interviewed. Firstly, a greater proportion of respondents were affiliated to a religious grouping (76% Christian and 20% Muslim). A number of studies have highlighted that religious affiliation do not only provide the norm and social glue for networking, but also fosters cooperation [49]. Thus, religious affiliation is one of the social capital available to women

entrepreneurs. Secondly, convergence was noticed in terms of the respondents educational levels. A greater proportion of the respondents have secondary school education (34%) and higher education with either Certificate, Diploma and first Degree (64%). Only 2% had attained basic education. The educational characteristics support the conventional view that education has an impact on entry into the formal economy [48].

An interesting characteristic of the respondents interviewed is related to their marital status. Broadly divided, the study found that 44% of the respondents were married and living with their spouses while 66% were living without spouses as either never married, widowed and divorced. The large proportion of women living without spouse demonstrate that more single women have become bread winners through running a business. This situation presents a good milieu for exploring spaces that single women employ to survive in a society that is heavily patriarchy [49].

### 3.2. Progress Within Oppression: The Gendered Distribution of Business Enterprises

The integration of women into the formal economy cannot be adequately understood without outlining the sectors in which women owned SMEs operate. While the policies paint an imagery of women owned SMEs integrating into the formal economy, empirical evidence from this study shows that this integration is largely within feminine dominated sectors. The survey conducted reveal that 86% of the respondents are running businesses that are considered feminine i.e. beauty industry comprising saloons, clothes, cosmetics (56%) and food industry comprising restaurants and catering (30%). The remaining 14% are running businesses in transport, construction and Information Technology (IT) sectors. The findings from this study demonstrate that contrary to the widespread policy view that women are being integrated into the formal economy, the formal economy is integrating women economic activities.

Thus, this paper argues that the efforts at integrating women business into the formal economy is characterized by a crash of interest. In particular, while the policy stipulation is to placate women into believing that it serves their interests, its practical implementation is to widen the formal economy. According to interviews conducted with women entrepreneurs that have just been formally registered, the hidden drive for promoting women integration into the formal economy is to broaden the tax base for the government. Thus, women entrepreneurs feel the outcomes of their integration belie their expectation of growing their business through accessing the needed financial capital, managerial skills and market opportunities.

### 3.3. New Wine in Old Bottles: The Case of Bonding and Bridging Social Capital for Accessing Business Opportunities for Women SMEs

Integration of women owned SMEs into the formal economy is justified as a means through which women would

access investment capital, business information and market opportunities required for growing their business [27]. In line with this reasoning, the general consensus among technocrats is that without being integrated into the formal economy, women owned SMEs cannot successfully grow their businesses. The understanding is that women participation in the informal economy lack the required social capital to access formal information, financial capital channels and credit associations. Thus, the understanding is that integration of women owned enterprises into the formal economy will enable them develop the required relations, networks, norm and trust for accessing business information, skills and financial capital [45].

However, these claims lacks credible evidence. The empirical evidence of registered women owned SMEs in Malawi reveals that women continue to predominantly use bonding social capital that they depended upon in the informal economy. For instance, 79% of the interviewed respondents reported depending on families, friends and informal business associations for business information and opportunities. A clear example is the use of their friends to authenticate the quality of products. Some of the women interviewed in this study specifically argued that *"we depend on our friends to direct us where to buy good products, especially when buying from outside the country; our friends link us with companies that sell quality products that we need"*. The findings from this study, therefore, belie the understanding that strong bonding capital is incompatible with the running of the formal economy [29], [40]. It should however, be noted that bonding social capital in terms of relations of reciprocity and trust do not widen but sustains the already existing market base. This is so as women sustain business associations that are already within their known circles. This finding, therefore, put into question the extent to which bonding social capital can restructure the formal market to the benefit of women.

Equally important, evidence from this study reveals that informal networks are heavily used by women-owned SMEs in getting customers and employees. For instance, 70% of the respondents reported that family, friends and walk-ins networks are a major source of their sales and labour to employ. While women owned SMEs have adopted advertising as a way of promoting their business, findings from this study reveal that the mode of advertising is largely informal i.e. advertising amongst the women's groups, neighborhoods and informal business associations. This finding mirrors Seevers et al [40] and Johansson [26] arguments that SMEs personal relationships with customers generate considerable customer referrals by circulating favorable information concerning the business. Women reliance on bonding social capital for accessing business information and opportunities can be explained by high information asymmetry in the formal economic sector.

#### **3.4. Deceived Promises: The Struggle for Business Capital for Women Owned SMEs**

Access to capital was one of the justification for the integration of women owned SMEs into the formal economy.

This understanding is based on the assumption that formally registered business entities develop bridging capital to negotiate capital for investment with formal financial institutions such as commercial and investment banks. Assessed against this variable, women integration into the formal economy can be described as deceived promises. This paper specifically argues that women were coerced into the formal economy by providing them with initial incentives that are not sustained overtime. For instance, while 24% of the respondents accessed their initial capital from formal financial institutions, only 10% continue to access capital from these institutions after registering their businesses. This means that 90% of the women owned SMEs continue to access business capital from the informal financial sector, especially group savings and lending, equal monthly rotating payments and informal money lenders. One common characteristic of all these financing mechanisms is that they depend on the existence of bonding social capital i.e. people loan to and get finance from individuals whom they trust that will pay back the loan.

Equally important, this study revealed that registration of their business has not correspondingly increased their access to formal market. On the contrary, they still largely depend on the informal market that they used before. The findings from this study, therefore, belie the existing literature that argues that financing mechanisms and market opportunities for enterprises shift from informal to formal sources as the business grows [2]. The understanding is that informal financing mechanisms and market opportunities become ineffective to meet the needs of formal business enterprises. These findings are in line with those of Aryeetey [5] who argues that in Africa there is little or no financing progression from informal to formal sources of capital as the business grows.

During focus group discussions, women particularly lamented that formal financing mechanisms are not open to them as they demand a lot of requirements. The participants argued that *"most financial institutions require guarantee to back our credit obligations and most of us do not have individuals and institutions to back our credit obligations, where do they think we can get the guarantors"*. This paper argues that the case of women integration into the formal economy and their continued dependence on informal sources of capital presents a classic case of the women lack of bridging capital needed to survive in the formal economy.

#### **3.5. Challenges Women-Owned SMEs in Conducting Their Business**

Although integration of women-owned SMEs potentially widens their market base, evidence from this study indicate that women continue to experience a number of challenges that threaten the prospect of establishing sustained business enterprises. The rest of this section expounds the challenges that have characterized SMEs and how these challenges have actually undermined their prospects for successful women entrepreneurs integration into the formal economy.

### 3.5.1. Limited Knowledge and Skills for Managing a Formal Business

This study has revealed that the integration of women-owned SMEs into formal economy has exposed women entrepreneurs to new challenges associated with formal market operations. These include record keeping, tax payment compliance, advertising, procurement and supply mechanisms. According to the focus group discussions conducted with women entrepreneurs, most women are just learning the new ways of running formal business and transactions. For instance, women explained that the process of acquiring loans from the financial institutions demands that their businesses submit a viable business plan to the lender and clear record of its past and expected cash flows and return prospects. This situation requires that women entrepreneurs be trained in business planning and management [9], [21]. According to the survey results, 62% of the women interviewed lacked the required business plan writing skills and record keeping. Equally important, the study revealed that about 58% of the women interviewed have not received any form of formal training in business management.

### 3.5.2. High Cost of Capital and Doing Business

Access to investment capital is one of the critical challenges that women entrepreneurs face in being integrated into the formal economy. According to the interviews conducted, 74% of the respondents continue to utilize informal sources (relatives and friends) to access investment capital, which means that only 26% used capital from the formal financial sector (commercial banks). The study also found that all the 26% who accessed loans from the commercial banks were working and banks gave them loans on the assurance of their continued monthly salary deposits. This study reveals that unless they have other collateral, individuals who purely depend on business face a lot of challenges in accessing investment capital. This finding mirrors a number of existing studies that argue that start-up investment capital in Africa is secured from informal sources [5]. Considering that women have not developed adequate bridging social capital in business operations, women entrepreneurs are likely to continue depending on informal sources of capital. This situation has an impact on the performance of women enterprises as initial undercapitalization negatively affect business performance [31].

Equally important, the few individuals that get investment capital from the commercial banks are subjected to high interest rate that make loan repayment difficult. Likewise, women SMEs' profits is eroded due to high utility cost especially to new businesses as they cannot enjoy the advantages associated with mass transactions. This is largely so as Malawi continues to suffer from longtime structural and productivity bottlenecks such as weak resource endowments, overdependence on rain-fed farming, high transportation costs and vulnerability to international shocks. These economic trends have resulted in the country experiencing high inflation rate of about 20%, high bank lending rate of about 34% and high unemployment levels of about 20.0% [35].

### 3.5.3. Patriarchal Elite Capture of the Market

Discussions with women entrepreneurs have revealed that the market in Malawi is heavily captured by the patriarchy system which has established unfair business competition. Women explained that they find it very difficult to access business information through the formal channels arguing they are not given full information or at times not even attended to. A clear example is where clients address women entrepreneurs as workers and not owners of the business. Interviewed women reported that *"men usually ask for sexual favors in return for business information"*. Equally important, some clients do not want to develop close business relations with women arguing *"I do not deal with women because people misinterpret our transactions for something else. Some women are also not trustworthy, they are used by other people to get information from you"*. These findings indicate that the market has been captured by a patriarchy system that makes it very difficult for women to do their business.

The findings from this study, therefore, reveal that while there is a general approval of women to get integrated into the formal economy, the system is not ready to transact business with them. This paper argues that in order to get integrated into the formal economy, women requires bridging social capital and not just the bonding social capital. This situation brings in a dilemma about creating bridging social capital where it does not exist. This paper argues that unless policy visions are accompanied by clear policy enforcement mechanisms, bridging social capital and thus women integration into the formal economy will not be achieved. This is so because, like any other social capital, the process of building bridging social capital produces winners and losers based on existing power structures [49]. It is, therefore, doubtful that women-owned SMEs will be successfully integrated into the formal economy in Malawi given the lack of clear policy enforcement for the increased participation of women-owned enterprises in the economy. Thus, the broader position of this paper is that women SMEs have been approved but not contracted.

## 4. Conclusion

Integration of Women SMEs into the formal economy is justified of the assumptions that it will increase women SMEs access to investment capital, business opportunities and widen their market base. Employing the social capital concept, this study examines the challenges and benefits of women integration into the formal sector in Malawi. The findings from this study reveals that, while women integration into the formal economy has the potential to increase women access to investment capital, business information and market opportunities, lack of bridging capital grossly limit the extent to which they can benefit from the integration.

This study has revealed that women have strong bonding social capital that they have been using in running their business. They have particularly used close relatives and friends to access investment capital, business opportunities, markets and trusted employees. This study has found that the

integration of women SMEs into formal economy has not changed this situation. On the overall, women SMEs face three challenges in getting integrated into the formal economy namely: lack of bridging social capital, high cost of investment capital and of doing business, and existence of a highly patriarchy market system. Thus, while women SMEs have been approved to get integrated to the formal economy, they have not been contracted. Therefore, unless complimented by deliberate enforcement mechanisms, rhetoric about women integration into the formal economy should not be expected to significantly improve the business performance of women.

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