Small and medium-sized forestry enterprises

Are they the best bet for reducing poverty and sustaining forests?

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SMALL and medium-sized forest enterprises (SMFEs) are poorly understood and difficult to define. They are diverse, and the dividing lines between them and micro- or large-scale enterprises differ from place to place. A working definition of an SMFE is: a business operation aimed at making a profit from forest-linked activity, employing 10–100 full-time employees, or with an annual turnover of US$10,000–US$30 million, or with an annual roundwood consumption of 3,000–20,000 m³.

Local enterprise: a logging truck is ready for unloading in a village in Mozambique.
Photo: D. Macqueen

Why are SMFEs important?

In the tropics, most forest products are produced and consumed locally. For those products that are sold, the domestic market dominates. It is commonly estimated that about 85% of wood from tropical forests is used for fuel, about 10% is timber used locally and about 5% is timber that is exported. Whilst exports are generally the preserve of large-scale enterprises, the domestic market is dominated by SMFEs.

Good information on SMFEs is scarce. Some rough extrapolations from existing information suggest that:

- in many countries, 80–90% of forestry enterprises are SMFEs;

- in many countries, over 50% of all forest-sector employment is in SMFEs;

- over 20 million people are employed by SMFEs worldwide; and

- over US$130 billion/year of gross value-added is produced by SMFEs worldwide. By comparison, the total global value of imports of wood-based products is about US$141 billion/year—most of which is produced by large enterprises; there may be an additional 140 million people working in informal forestry micro-enterprises, mainly in developing countries.

Why have SMFEs been so ignored?

SMFEs are diverse, informal, slippery and risky. They pose difficulties for policy-makers because of:

- the complexity of establishing links with diverse SMFEs in multiple locations;

- the diversity of constitution of SMFEs, which reduces the likelihood of common agendas;

- the small individual scale of each enterprise, which reduces the per-unit impact of interventions;

- the volatility of economies in which they operate and hence their necessary flexibility, mobility and opportunism;

- their lack of resources for dealing with bureaucracy and their lack of political muscle for beating the system; and

- the fact that SMFEs are risky business. They often have informal business patterns, insecure tenure or resource access, low managerial and technological capacity, and little collateral.

SMFEs often have weak relationships with external investors and a lack of capital to offset these risks themselves. It is estimated that some 80% of SMFE financing comes from the owners themselves, their friends and their families. SMFE owners are thus the dominant 'investors' in forestry.

What are the environmental and social impacts of SMFEs?

The influence of SMFEs in communities varies considerably depending on the setting, but a few general comments can be made.

- The conditions under which SMFEs work—informality, insecure tenure, low investment, low profitability—may reduce their scope for taking account of environmental concerns. However, sometimes local accountability can improve environmental quality: eg in patchwork landscapes based on smallholder production.

- Most social benefits occur where both larger enterprises and SMFEs co-exist and where the employment share of

SMFEs increases at the same time as improvements are made in technology and standards resulting from the links between the SMFEs and larger enterprises.

- Fewest social benefits arise when there is 'distress diversification'—where poor people with few other options seek refuge in low-skill activities and seasonal labour migration.

- SMFEs may make a positive transition to larger-scale enterprises, or they may be replaced by large firms with distant product sourcing and repatriation of profits elsewhere.

Are SMFEs a good thing?

Generally, SMFEs play a positive role, and they are not going away.

- There is evidence that SMFEs usually generate net benefits: by playing a key role in providing basic needs, often part-time with other activities; by spreading wealth locally; by empowering local creativity; and by preserving cultural identity (but there are also examples of socially disastrous SMFEs).

Sales pitch: women sell custard apples by a roadside in India. *Photo: Andhra Pradesh Forest Department*

- SMFEs are better than large enterprises at understanding local political contexts, linking with local civil society, and committing to operate in a specific area.

- Rather than ignoring SMFEs, there is a need to build on their strengths and deal with their weaknesses.

What prospects for greater investment in SMFEs?

- Where taxes are high, regulations numerous and unfairly applied, and revenues appropriated privately, there is a high incentive for SMFEs to stay outside or leave the formal economy.

- Corruption and illegality go hand in hand in many forest frontier areas where SMFEs predominate.

- SMFEs are often notionally subject to multiple government authorities—who may be badly connected, frequently changing, and disdainful of SMFEs.

- Decentralization and co-management arrangements hold much promise.

- Consumer concerns for fair trade have the potential to support what is best in SMFEs.

- Where SMFEs group together in clusters or associations they can play a greater role in securing investment, articulating needs and influencing policy.

Recommendations

- **Foster enterprise associations and support their specific needs:** associations can shape the policy environment, reduce transaction costs and invest in adaptive strategies. Targeted support can bring major rewards.

- **Simplify and stabilize laws and enforce them equitably:** in some cases, clear titling helps. In others it is the democratic involvement of marginalized groups in decisions over common land that is critical.

Policies that foster a competitive but also vertically mobile SMFE sector are preferable to those that merely protect them.

- **Support judicious subsidies, and remove unreasonable subsidies and trade barriers:** these may be vital additional tactics where there are good grounds for opposing the accumulation of power in the hands of a few.

- **Develop credit unions and better risk assessments:** credit unions can play a vital role in making efficient use of the capital held by individual SMFE owners. Group-lending contracts with joint liability hold much promise, and group certification can also help unlock credit lines. Risk assessments that reflect forest timeframes and constraints are needed if banks are to deal more effectively with SMFEs.

- **Build capacity for management, deals with larger players, and to broker finance:** developing capacity for managing appropriate business models with larger firms may be vital as a route to investment finance. Brokering bodies to connect SMFEs with policy initiatives, investment sources and business support agencies are emerging in some countries, and viable approaches need to be further developed and spread.

Conclusion

If we accept that forestry can and should do more for sustainable development and poverty reduction, then we must do better than looking for answers solely in large or micro-scale enterprises. We need to look more at the kinds of enterprise that actually exist and make up the majority of the forest sector—the SMFEs. We need new financing mechanisms for building on the investments of responsible SMFE owners. The best chance for success lies in strengthening SMFE associations.

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